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INTERNATIONAL AIR ROUTE CERTIFICATES

HEARING

BEFORE THE

SUBCOMMITTEE ON AVIATION

OF THE

COMMITTEE ON COMMERCE, SCIENCE,
AND TRANSPORTATION
UNITED STATES SENATE

NINETY-NINTH CONGRESS

FIRST SESSION

ON

S. 586

TO PROVIDE FOR THE REVIEW OF CERTAIN AUTHORITY IN CERTIFICATES ISSUED UNDER THE FEDERAL AVIATION ACT OF 1958, AND FOR OTHER PURPOSES

MAY 23, 1985

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INTERNATIONAL AIR ROUTE CERTIFICATES

THURSDAY, MAY 23, 1985

U.S. Senate,
Committee on Commerce, Science, and Transportation,
Subcommittee on Aviation,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:35 a.m., in room SR-253, Russell Senate Office Building, Hon. Nancy Kassebaum (chairman of the subcommittee) presiding.

Staff members assigned to this hearing: Chuck Doyle and Steve Johnson, staff counsels; and Steve Palmer, minority professional staff member.

OPENING STATEMENT BY SENATOR KASSEBAUM

Senator Kassebaum. The hearing will come to order.

The hearing this morning is on S. 586, a bill which would transform all temporary international aviation route rights into rights of indefinite duration. It is a bill that Senator Inouye has been interestd in for some time. I think it is an important piece of legislation.

I have a statement from Senator Hollings for the record.

[The statement and bill follows:]

Opening statement by Senator Hollings

Today's hearing presents an opportunity for the Aviation Subcommittee to review an issue that was widely discussed last year, as the Civil Aeronautics Board went out of extistence. Near the end of the 98th Congress, there was a push to enact legislation similar to S. 586, which my friend from Hawaii, Senator Inouye, has introduced. However, after much discussion, an agreement was reached to hold off on consideration of legislation relating to international airline certificate duration until after hearings could be held, which the Subcommittee Chairman and the Ranking Democrat agreed to do early in this session.

International air service has become an important profit center for U.S. carriers. In a recent year, 40 percent of all industry operating revenues were derived from service to foreign markets. It comes as no surprise, therefore, that the carriers now in those markets want assurances that those resources will not be taken away from them.

S. 586 would do just that. It would make all existing international airline certificates permanent, eliminating the need for periodic review of the adequacy of service. It would also attempt to strengthen the language allowing the Department of Transportation to remove an incumbent carrier, should its level of service deteriorate beyond repair.

At first glance, this concept has some attraction. It would help the airlines develop valuable long-term resources. It would help them minimize costs. And it would provided an even playing field for the individual carriers by not allowing some carriers to operate under permanent certificates, while others are subject to periodic renewal.

Other groups, notably those with consumer ties, have expressed some concern over this concept, arguing that it will be anticompetitive and could encourage carriers to become lazy and indifferent in the quality of service they provided. S. 586, they contend, would provide no benefit to the air traveler.

The debate on this issue has been lively and interesting. I am hopeful that that tenor continues at today's hearing. I have looked over our witnesses prepared statements, and I am looking forward to their responses to Committee questions on this issue. The input of these experts will thus help us make our decisions in shaping legislation in this area of aviation policy.

99TH CONGRESS
1ST SESSION

S. 586

To provide for the review of certain authority in certificates issued under the Federal Aviation Act of 1958, and for other purposes.

IN THE SENATE OF THE UNITED STATES

MARCH 5 (legislative day, FEBRUARY 18), 1985

Mr. INOUYE (for himself, Mrs. KASSEBAUM, Mr. EXON, and Mr. DANFORTH) introduced the following bill; which was read twice and referred to the Committee on Commerce, Science, and Transportation

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A BILL

To provide for the review of certain authority in certificates issued under the Federal Aviation Act of 1958, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 401(d) of the Federal Aviation Act of 1958 (49 App. U.S.C. 1371(d)) is amended by adding at the end thereof of the following:

"(10)(A) On and after the date of enactment of this paragraph, a termination date in any certificate to engage in foreign air transportation which was issued under this section and is in effect on such date of enactment shall have no effect.

"(B) The Secretary of Transportation may, upon application or on the Secretary's own motion, review the authority to provide foreign air transportation between a particular point or points in any certificates to which subparagraph (A) of this paragraph applies. The Secretary may suspend such authority, and grant authority to provide such foreign air transportation to a qualified applicant for such authority, if the Secretary finds, after notice and an opportunity for a hearing on the record, that the applicant has demonstrated that it can and will provide a substantially improved combination of service and fares or rates in the market or markets, and if the Secretary finds that—

"(i) restrictions arising from the provisions of a bilateral air transport agreement or other agreement or understanding with a foreign country, or otherwise imposed by a foreign country, preclude or make it impracticable for the Secretary to authorize an additional carrier in a particular foreign air transportation market or markets; and

"(ii) suspension and grant to the applicant of such authority would otherwise be consistent with the public convenience and necessity.

"(C) The Secretary may dismiss any application for suspension and grant of authority under subparagraph (B) of this paragraph if the Secretary is not satisfied from the materials submitted with the application that—

"(i) the applicant is qualified;

"(ii) it is probable that the applicant could and would provide substantially improved air service in a restricted market; or

"(iii) proceeding with consideration of the application would otherwise be in the public interest.

"(D) The authority of the Secretary under subparagraphs (B) and (C) of this paragraph shall be in addition to, and shall in no way limit, the Secretary's existing authority under paragraph (8) of this subsection or under subsection (p) of this section.".

Senator KASSEBAUM. It is a pleasure to welcome as our first witness this morning a former member of our committee, Senator Lautenberg.

STATEMENT OF HON. FRANK R. LAUTENBERG, U.S. SENATOR FROM NEW JERSEY

Senator LAUTENBERG. Thank you, Senator Kassebaum.

I apologize for my tardiness. It is a pleasure to appear before you, Madam Chairman. The meeting is starting very close to on time. It is a precedent that I am sorry to upset.

Madam Chairman, Senator Inouye, it is a pleasure to appear before the Aviation Subcommittee, on which I served during the 98th Congress. I continue to have a deep interest in the issues within the subcommittee's jurisdiction.

One such issue, the one before you today, the awarding of international air route certificates, is one that I am quite concerned about. The issue, while technical in nature, will have a major impact, I believe, on America's airlines and America's consumers.

With the passage of the Airline Deregulation Act of 1978, low-cost air travel became available to the traveling public. The introduction of competition into domestic air travel has been a success.

While there remain problems with providing essential service to smaller, more isolated communities, those problems can be addressed within a framework which enhances competition and provides low-cost service options to consumers.

In international aviation, we simply cannot decide to deregulate and maximize competition. International routes are still heavily regulated by foreign governments. A number of countries do not limit access to their markets. Where this relatively competitive situation occurs, no effort on our part is necessary to induce competition.

However, in those markets where access is restricted, like Spain and Canada, an effort is needed to enhance competition. That is why we have these 5-year temporary certificates. Carriers are granted 5-year periods to provide service.

At the end of that period, their performance is reviewed. If they have done what they said they would do, then they were awarded the route, and when they were awarded the route, they will keep it.

If they have not maintained the route as they said they would, they might or might not lose the route, depending on the likelihood of another carrier providing the same or better service.

We have temporary certificates to ensure that some competitive pressure is applied and monopoly situations do not occur. The question is, does this existing system serve the public well, or should it be changed?

It is the purpose of S. 586 to fundamentally change this procompetitive environment and convert all temporary authority to permanent status, freeing incumbent carriers from competitive pressures.

I do not think the Congress ought to take this step. A similar proposal was considered in the House during the 98th Congress, in the House Aviation Subcommittee. It carefully examined the issue, and it took no action. The more this issue is studied, the more apparent it becomes that this bill is antithetical to competition and not in the interest of the American consumer.

Madam Chairman, do we need to fix what is not broken? Have compelling arguments been made to justify taking this step? The major arguments in favor of providing blanket permanent certificates is that doing so saves the carriers time and money. It is said that no incumbent carrier has ever lost a route.

Those are legitimate concerns. We should not be adding costs to airlines just to create problems or give people at DOT something to do. But I would caution the Committee to examine all the costs and benefits of this legislation. If the existence of competition results in costs to the carriers, the lack of competition will result in greater costs to the public.

The case most often cited by the proponents of the bill is the trans-Atlantic route proceeding, which took years to resolve, and cost $500,000 in legal fees. But as the House hearings made clear last year, that proceeding involved dozens of routes, and the cost on a per route basis was quite reasonable, given their value to the carriers.

This case was also considered in a prederegulation environment which would not occur again today. Sure, it costs money to defend these routes, but this is a very lucrative business. About 40 percent of the industry's profits come from these routes.

As for the point that no route has been lost, that is because Congress has extended this temporary authority through legislation, and therefore no route has actually yet to be defended.

In one of its last actions, the CAB extended temporary certificates for 12 to 14 months. In considering this issue, one House Member had an appropriate analogy. He said the present system of having to defend your performance reminds him of an election. To the incumbent, an election is inconvenient indeed.

All those promises to account for and a record to defend sometimes make it difficult. Lord knows, it costs time and money. Would it not be wonderful if we could get permanent certificates? We would not have to worry so much about providing service, and that might be good for some incumbents, but it would be awful for the American people.

The removal of competition in international aviation will be equally bad for American consumers.

I am not in favor of saddling our airlines with additional costs and regulations. DOT can and should reduce the time and expense of route renewal cases while preserving a competitive environment.

This subcommittee should encourage such efforts, but this legislation goes further than that by insulating the incumbent carriers from competition.

Where routes involved bilateral agreements between the United States and a foreign country, the Departments of State and Transportation hold the public's proxy in securing those routes for the benefit of the nation and the traveling public.

These routes are a public resource. Making all of these routes permanent will make them virtually the private property of the carriers to be sold then to the highest bidder.

In New Jersey, airline deregulation has meant that those who previously could never afford to fly now have that option. We have begun to see low-cost international travel as well, and I believe that the enactment of S. 586 will nip that low-cost option in the bud.

Newark Airport is one of the fastest growing in the Nation, the fastest growing in the New York region. Low cost international travel is part of that growth, and I would like to see more low-cost flights out of Newark and other airports to more foreign destinations.

S. 586 could well preclude that growth. Some carriers might be concerned about blocking in routes that carry international business travelers on expense accounts. My concern is for the person who has never been able to go overseas because fares were prohibitive.

Competition serves the traveling public well, and I believe it is our responsibility to preserve competition whenever possible. For that reason, I hope that the subcommittee will reject S. 586. Thank you.

Senator **KASSEBAUM**. Thank you very much, Senator Lautenberg. Your comparison to an election and an incumbent is an interesting one. My apologies. I forgot to ask Senator Inouye if he had an opening statement. Senator Inouye?

OPENING STATEMENT BY SENATOR INOUYE

Senator **INOUYE**. I thank you very much.

Madam Chair, this morning we are considering a measure to address an outdated and counterproductive aspect of our national aviation policy which I believe is creating inequities and inefficiencies for the airline industry. Since airline deregulation and the subsequent sunset of the CAB, most of the burdensome regulations and bureaucracies have been eliminated.

However, one has not been eliminated, and that is the system of awarding international route certificates. At the present time DOT may award some international route certificates on a periodic basis. On certain closed routes, this results in some airlines holding temporary certificates while others hold permanent certificates for the same route.

And obviously, this procedure has caused inequities and distorted market competition. Under the present system an airline holding a temporary certificate must face route challenges every 3 to 5 or 7 years, regardless of his service record, and as pointed out by the Senator from New Jersey, these challenges sometimes require costly defenses by the incumbent carrier, and have never resulted in a transfer of routes.

A recent renewal proceeding cost the incumbent airline $500,000. And it is true that there were several separate routes, but it is an expense I am certain that was passed on to the consumer. The bottom line on current international certificates policies is that it is an unnecessary burden.

The deregulated airline industry is already moved by market pressures which induce airlines to attract customers with superior fares and services. Many international routes, the Pacific and

South American, are heavily regulated with fixed fares and limited numbers of flights.

In such an environment, a carrier has minimal flexibility, and the consumer's choices are by nature limited. Under these conditions, you would tend to hurt the consumer by replacing an established carrier with one whose continued service is less certain.

Since the advent of airline deregulation and the subsequent sunset of the Civil Aeronautics Board [CAB], many burdensome regulations and bureaucracies have been eliminated. One that has not been eliminated, however, is the system of awarding international airline route certificates. Under section 401 of the Federal Aviation Act, the authority exists for the CAB, and therefore its successor agency the Department of Transportation, to award some international route certificates on a periodic basis. On certain closed routes, the CAB has used this authority to award temporary certificates to some airlines while others held permanent certificates for the same route. This procedure has been applied inconsistently from administration to administration and has caused inequities while distorting market competition.

The examples of inequity created by the current system are quite obvious. For instance, on routes to Italy, Transworld Airlines [TWA] holds permanent certificates while Pan American World Airways has only temporary authority. On routes to Great Britain, however, TWA holds temporary certificates while Pan American enjoys permanent status. The reason for this and other discrepancies is merely that different CAB administrations have applied section 401 in different ways. The result is distorted competition on these important routes.

Under the current arrangements of section 401, an airline holding a temporary certificate must face costly route challenges every 3 to 7 years regardless of its service record. These challenges require costly defenses by the incumbent carrier and very rarely result in the transfer of routes. Indeed, to my knowledge there is only one significant example, that being the CAB's removal of Pan American from its Scandinavian route in 1978. In that case, however, the airline was preparing to drop the route anyway, so the CAB action was merely a formality. On the other hand, renewal cases are almost always expensive. One recent certificate renewal cost an incumbent airline $500,000; an expense that was undoubtedly passed on to the consumer. In addition, the length of these temporary certificates is too short for an airline to recoup its investment in a route and thus makes it difficult for that airline to make the policy decisions necessary to get established on that route.

The bottom line on current international certificates policy is that it is an unnecessary burden. The deregulated airline industry is already moved by market pressures which induce airlines to attract customers with superior fares and services. The threat of periodic renewals does little, therefore, but marginally enhance existing market pressures. It is important to note, also, that many of the international routes involved are heavily regulated with fixed fares and limited numbers of flights. In such an environment, a carrier has minimal flexibility and the consumers' choices are by nature limited. Thus to take out an incumbent carrier and put in another who will be subject to the same stringent regulations does little to enhance the consumers' position. Indeed, it would tend to hurt the consumer by replacing an established carrier with one whose continued service of the route is less certain.

To address the situation I have described here, I have introduced legislation, cosponsored by the lovely chair and Senators Danforth and Exon which would transform all current temporary route certificates to an indefinite status. To assure that this will not in any way be anticompetitive, the legislation also strengthens and defines the procedure by which the Secretary of Transportation can replace a carrier which is providing relatively inferior service on a route. Thus if the incumbent airline is abusing its route privileges and/or another airline proves it could provide better service on the route, the authority would exist for the Secretary to replace the incumbent carrier. This could be done by application of another carrier or by motion of the Secretary. This is in addition to existing authority established in the Federal Aviation Act allowing the Secretary of Transportation to review carrier performance and replace negligent carriers.

This legislation will in no way effect the State Department's ongoing negotiations to increase international route authority for U.S. carriers. These negotiations have historically been the means by which domestic carriers have been able to enter new routes. Petitioning to replace an incumbent carrier on a route is only resorted to when these negotiations are delayed or proven fruitless. In the majority of cases, however, where it is proven that an additional carrier can service the route effectively, the State Department has been successful in securing that route authority. A recent example of this is People Express Airlines' entry into the Newark to London market as a result of U.S. Government intervention.

In closing I would like to stress this legislation's importance in streamlining the post deregulation aviation environment. By correcting inefficiencies and inequities in the current system, this bill will allow U.S. airlines to better compete with foreign carriers, none of which are subject to temporary route renewals. This bill will also clearly and strongly define the Secretary of Transportation's authority to replace carriers on routes they are serving inadequately. I believe that this is better aviation policy than forcing airlines who have served a route responsibly and effectively for years to jump through hoops which almost never result in improved service but which always involve costly paperwork and redtape cutting.

Thank you very much.

Senator **KASSEBAUM**. Do you have any questions for Senator Lautenberg?

Senator **INOUYE**. I have been told we are not supposed to ask Senators questions.

If I may, just one question. Some have suggested that section 401, the so-called bumping procedure, is not adequate because the procedure calls upon the challenger to prove that the incumbent is not doing a good job. Do you think that this section is inadequate?

Senator **LAUTENBERG**. I think there is a question about whether the procedure actually works as it should. I think what the challenger has to do under that procedure is to establish, and certainly it has got to be hypothetical, that they would be able to provide better and cheaper service.

I think that is always a very subjective analysis. I believe that regular review takes the uncertainty out of a bumping type challenge. Certainly, it would not be difficult for the carrier providing the service to establish on the record their ability to provide service at decent prices, convenient schedules, all of those things.

I think that the bumping procedure interrupts the possibility that we can have an orderly process in being, and not do what I used the election reference as an example for, and that is, in the last year, in the last moments, somehow or another attendance often becomes more diligent, communications with constituents, et cetera.

Well, I think the same thing is true, Senator Inouye, in the airline business. We are liable to see a beefing up of service at a time when the challenge comes, but if you examine the record on a regular basis, you know whether the service has been there.

Senator INOUYE. Is it not also true that in all endeavors in the American society, whether it be business or in the courtroom, that it is the requirement of the challenger to bear the burden of proof that the incumbent is either guilty or not doing the job, and why in this case should the incumbent have to demonstrate that it has done a good job?

Senator LAUTENBERG. Well, because we know very well that this is a limited resource. I think where there is unlimited ability to compete, then certainly one need not to have to prove anything except to the consumer that they can provide the service. But in this case it is different, because if a foreign nation permits only one flight a day from a given airport, or two flights a day, I think it makes it awfully difficult for a competitive service to really be offered. And so I would disagree respectfully with my colleague from Hawaii that the comparison is the same.

I think that in the marketplace the way we challenge is with free competition, and one need only look at the routes from the New York area down here and see what happened to the fares when we had a new entry come into the marketplace under deregulation.

It just changed the whole ball game, increased the traffic substantially. People fly who could not fly before. And that is always the best testing ground, I think. And free competition. If we had that in the unlimited access markets, why, there is no question about it. But where we have a limited access, I do think we have to impose, unfortunately, the hand of Government.

Senator INOUYE. I, too, have sensed the possible inadequacy of 401, and so I am certain you will agree that the bill that we have introduced will strengthen the hand of the Secretary and make the so-called bumping procedure much easier.

Even if the burden is still on the challenger to prove that the incumbent is not doing a good job, the Secretary's hand has been strengthened, so it would make that procedure much, much easier. That is what we tried to do. It is an important aspect of this bill.

Senator LAUTENBERG. I agree with the Senator that that is an important aspect. However, I think that once and for all we ought not to have any doubts about whether a given administration or a given Secretary or a given department has any kind of a bias or a preference.

I think if it is clearly left to be judged on the record in a timely fashion, I think that is the best of all possible worlds.

Senator INOUYE. I thank you, Senator.

Thank you, Madam Chairman.

Senator KASSEBAUM. Senator Ford.

Senator FORD. No questions. Thank you.

Senator KASSEBAUM. I think one thing that I will be wanting to explore further is really the situation that does exist in many routes with the permanent and the temporary certificates, how that works, and if that is a problem. When we talk about competition, which is what we were attempting to achieve in many markets you do have differentials that exist. How did that come to be and how does that affect the particular situation?

Senator LAUTENBERG. One need only look at particular routes, and I still fly occasionally on the private side. I was abroad on a trip to Germany a couple of weeks ago, and I was astounded at the fare levels between cities in Europe where the markets are locked in. It is incredible how much higher they are than what a ticket for an equivalent distance would cost in this country.

Whenever you see restricted competition, the rates are very cushy. Whenever you see wide open competition, you see the result, and I think that is the way we have to look at it.

Senator KASSEBAUM. Thank you very much, Senator Lautenberg. It is a pleasure to have you back on the Commerce Committee.

Senator LAUTENBERG. Thank you very much, Madam Chairman and my esteemed colleagues who sit on this committee. I do miss serving with you.

Senator KASSEBAUM. The next witness is Mr. Jeff Shane, Deputy Assistant Secretary for Policy and International Affairs, Department of Transportation.

STATEMENT OF JEFFREY N. SHANE, DEPUTY ASSISTANT SECRETARY FOR POLICY AND INTERNATIONAL AFFAIRS, DEPARTMENT OF TRANSPORTATION

Mr. SHANE. Thank you, Madam Chairman and members of the subcommittee. I am very pleased to be here today to comment on S. 586 on behalf of the Department of Transportation.

This bill would nullify any termination date which is contained in an international air transportation certificate.

It would also provide a "bumping" procedure which is designed to facilitate the replacement of incumbents should the department find that another carrier can provide substantially improved air service in the market.

Presumably this bill was drafted in response to concerns that incumbent carriers are burdened by the cost of prosecuting automatic route renewal proceedings, and that they are unable in just 5 years—that is the term of the current generation of temporary experimental certificates—to develop international routes sufficiently to recoup their investment.

As the committee is aware, the Civil Aeronautics Board consistently issued temporary experimental certificates for limited designation routes after the enactment of the Airline Deregulation Act of 1978. Many of the outstanding temporary experimental certificates were scheduled to expire during 1985.

In November of last year, in anticipation of its impending sunset and the transfer of its international route responsibilities to the Department of Transportation, the Civil Aeronautics Board adopted an order extending the duration of most of those temporary international certificates for a period of 12 to 14 months.

The purpose of that extension was to allow the Department of Transportation time to undertake a comprehensive review of the issues involved in selecting carriers for limited designation international routes, including the question of whether certificates awarded on those routes should continue to be of limited duration.

In keeping with that objective, the Department expects in a very short time to issue a notice of proposed rulemaking asking for public comments on the issue of certificate duration.

Based upon the comments that we received, the Department may adopt a policy either of granting fixed term certificates for limited designation of routes or, on the other hand, of awarding certificates for an indefinite period subject to revocation under certain specified procedures.

Because we are about to begin a proceeding that would comprehensively consider the issue of certificate duration, the Department cannot support the adoption of S. 586. The Department takes the position that any action on the question of certificate duration should occur through the rulemaking process after the filing of public comments.

Indeed, this is the approach that we announced last year that we would follow, and it is the approach that the industry and the public at large are now fully expecting us to carry out. While I cannot, of course, publicly comment on the specifics of our notice of proposed rulemaking, I would like to take this opportunity to frame the setting for the central issue.

For those routes where the state of our bilateral aviation relations permits the United States to designate an unlimited number of airlines, the problem of certificate duration does not arise. In those situations, where the marketplace is allowed to operate relatively free of governmental restrictions, there is no reason to limit the duration of certificate authority.

Competitive forces will properly be the determinant of which carriers serve that particular market and for how long. Therefore the Department will continue to award permanent or indefinite authority to carriers desiring to serve these unrestricted markets.

Unfortunately, many of the international routes that involve heavy passenger and freight traffic are restricted to a limited number of U.S. carriers. Particularly I would mention the routes between various U.S. cities and gateway cities in Canada, the United Kingdom, Japan, and Mexico. Because these markets are of such value in terms of air traffic and revenues, they have been among the most hotly contested in carrier selection cases.

The U.S. Government has pressed foreign governments, and will continue to press them to permit the designation of an unlimited number of U.S. carriers. Nevertheless, it would be unrealistic to predict that most of those governments which currently impose a limitation on entry are likely to change their policies in the very near future.

Therefore we must be prepared to deal with the competitive implications of an artificially constrained market when making limited designation route awards. Our predecessor, the Civil Aeronautics Board, utilized temporary experimental certificates with a set termination date in an attempt to simulate some of the competitive forces that would operate naturally were unrestricted entry permitted in particular markets.

By limiting the certificate authority to a fixed number of years and defining it as experimental, the board sought to create an ongoing incentive to the incumbent to offer the best service possible in anticipation of potential challenges to its route authority and to follow its proposal as closely as circumstances permit.

At the same time this policy ensured that other carriers could apply for the route at some point in the future. The Department cannot say with assurance that the use of limited duration certificates has or has not accomplished these objectives.

This is precisely why we are determined to seek public comment on that question. There may be other approaches, such as that contained in S. 586, which can accomplish the same goals with less burden on certain incumbent carriers.

However, it also may well prove to be the case that there is no effective substitute for the competitive incentives created by an automatic review process. At this point we simply do not have a sufficient basis for drawing final conclusions about the efficacy of the limited duration certificate. The rulemaking will provide that basis.

We are hopeful that those interested parties who respond to our request for comments will help us reach a more complete understanding of both the advantages that the limited duration certificate provides, and the particular burdens that it imposes on incumbents, by providing specific data to support their claims.

Also, should a bumping provision be deemed necessary, the comments will also help us assess the relative merits of different options. We believe that the comments we receive will be valuable not only to the Department, but also to the subcommittee in its endeavor to assess the persistent question of certificate duration.

The Department therefore strongly recommends that the subcommittee postpone consideration of S. 586 for a short period of time while the industry and the traveling public are given the opportunity to comment, and the Department to respond, on this important issue.

Thank you. I will be happy to answer any questions you might have.

Senator KASSEBAUM. Thank you, Mr. Shane.

Senator Inouye.

Senator INOUYE. It is my understanding on certain international routes, some of the carriers have temporary certificates, others have permanent route authority. What is the rationale for this?

Mr. SHANE. Well, it was the case for many years that the Civil Aeronautics Board traditionally awarded, routinely awarded, permanent authority in all international markets. After the airline deregulation was passed in 1978, given the new provision that the act added to the Federal Aviation Act authorizing the Board to award certificates on an experimental basis, the Board chose that route. So that, as a result of the change in its legislative authority and also as a result of a change in the Board's policy over the years to try to simulate competition where it did not otherwise exist, the Board basically shifted courses. It simply had a different outlook and it had new legislative authority with which to implement that outlook.

Senator INOUYE. What did the CAB at the time of deregulation mean when they used the word "artificial" to describe the distinction between permanent and temporary, that there was no real distinction between temporary certificates and permanent authority, that the difference was just artificial?

What did they mean by that?

Mr. SHANE. Well, if I understand correctly, Senator, the adjective "artificial" referred to the kind of competition, or the competitive stimulus, that the Board was attempting to create through the use of the temporary experimental certificate.

Because entry was restricted by the terms of a bilateral agreement with a foreign government, the incumbent carriers would not have the kind of marketplace incentives to enhance their service proposals, to offer the lowest price service possible that they would otherwise have. By providing at a fixed point in time an opportunity for other airlines to challenge the authority of the incumbents, in effect the Board said that they would be holding the incumbents' feet to the fire.

If the incumbents did not act as though there were a competitive threat, then an aspiring new entrant would be able at such time as the temporary certificate were up for renewal to come in, put its case on the record, and have the CAB substitute it for the incumbent.

Senator INOUYE. Has any incumbent been removed as a result of the renewal proceeding?

Mr. SHANE. Not an incumbent in the usual sense. In a recent case, the Department of Transportation removed Pan American from the Houston-London market and substituted Continental. The reason I say that is not the usual case is that Pan American was not in fact operating on the Houston-London route at the time that that substitution took place. But there was, in effect, a substitution of designation. Continental now has an exemption from the Department of Transportation to operate the Houston-London authority.

Senator INOUYE. Do you think it enhances efficiency to have a group of carriers with temporary certificates and another group with permanent authority?

Mr. SHANE. Senator, I don't think it enhances efficiency. There is some question, of course, in our minds—and this is why we are putting out this notice of proposed rulemaking very shortly—about whether temporary certificates are the best approach to creating an artificial competitive stimulus of the sort that is needed in a restricted entry market.

If after considering the comments we determine that indefinite certificates with a bumping procedure, something along the lines that are suggested in S. 586, is the better approach, then of course that anomaly would be removed. All carriers would be operating on something like the same basis.

In the event that we determine, on the basis of the comments, that temporary certificates do seem like the best way to go, then I suppose that anomaly would persist. It is not clear to us on the basis of anything that we have seen yet that that anomaly has caused any serious problems in the market.

That does create an advantage, I suppose, for those incumbent carriers that are operating under permanent authority, but that advantage is only as good as their performance is. There are bumping procedures, as you know, in the Federal Aviation Act at the present time, which would be available to any aspiring new entrant.

Senator INOUYE. In drafting this bill, we tried our best to strengthen the hand of the Secretary in section 401, the so-called bumping procedure. And to bring this about we worked not only with the legislative counsel, but we conferred with attorneys in your Department.

Do you believe that we succeeded by this measure to strengthen the hand of the Secretary?

Mr. SHANE. Under section 401(d)(8) of the Federal Aviation Act, a provision that was added by the Airline Deregulation Act of 1978, the Secretary is authorized, where a certificate is experimental in nature, to revoke that certificate and introduce a new carrier on the grounds that the incumbent was not providing the innovative low-cost air transportation that it proposed to provide in the proceeding in which it was selected for that route.

So that the Secretary does have authority at the present time, at least as to incumbents operating under experimental certificates, which I believe is very similar to that which is contained in S. 586. S. 586, of course, would apply not only to experimental certificates but to all certificates.

I believe that the bill would provide greater leeway to the Secretary in the case of a permanent certificate, a carrier that was operating under a permanent certificate. If I can just offer a personal view about that new standard, however, again with the caveat that we are in the process of issuing a notice of proposed rulemaking and our minds are essentially open on all of these issues, I would express some concern that, to the extent that the bill enhances the Secretary's flexibility, it may provide encouragement for many aspiring carriers to come in and seek to oust incumbent carriers, not just at a 3-year or a 5-year or 7-year cycle when a temporary certificate expired, but at any point in time.

That troubles me from an administrative standpoint because, contrary to what some may assume, the Department of Transportation is not casting about for things to do. We have more than enough at the present time, and dealing with a lot of cases, many of which might be frivolous, is not in our view an efficient way to run the carrier selection process.

Second, in fact I believe that the prospect of those kind of efforts to oust incumbent carriers, because they would be coming in at any point in time and not just when a certificate expired, might very well prove to be more burdensome to incumbents than the present system is. There would not be any discipline, in other words, in the process.

Incumbents would not be assured, as they are now as a practical matter, of at least a 5-year period in which to establish themselves in a market to try different approaches, to try to test the market, to see what kind of a market it is, whether it is a low-fare discretionary tourist market or whether it tends to be mostly business traffic which tends not to be quite as price elastic.

There are a variety of approaches which may warrant a genuine test in the marketplace which it would be difficult to try if, because of a provision in S. 586 that enhances the Secretary's ability to oust incumbents, there were a fear that there would be an immediate application by an aspiring new entrant to oust the incumbent.

Senator INOUYE. Is not 401 available now to the Secretary and to aspiring airlines to bump temporaries, even 3 months after the temporary certificate has been issued?

Mr. SHANE. Yes; 401(d)(8) says that in the case of a temporary experimental certificate a showing that the incumbent carrier was not providing the kind of innovative service it proposed to provide——

Senator INOUYE. Have we had an avalanche of airlines seeking the 401 route bumpoff?

Mr. SHANE. No, sir, we have not.

Senator INOUYE. So what makes you think that with S. 586, this would happen?

Mr. SHANE. Only that the standard is broader and that the standard applies more to what the new applicant is intending to propose than what the incumbent is already providing. That is to say, an applicant would have to demonstrate under the provision, as I understand it, that it can and will provide a substantially improved combination of service and fares in the market, and that is a very subjective judgment, a judgment which would have to be based in the first instance on nothing more than another proposal, rather than any real test in the marketplace.

Senator INOUYE. But the burden is on the challenger.

Mr. SHANE. Yes, of course, as it is under the present law.

Senator INOUYE. Won't that enhance competition?

Mr. SHANE. It would enhance competition if it worked as the drafters of the bill expect that it would work.

What troubles me, Senator, is that it is not entirely clear that we would not find ourselves with, under this provision, the kind of rash of applications which we have not had under present law. I am speculating. I don't know that that would be the case, but at least the possibility exists that we would find ourselves with a less disciplined process than we have at present, with a greater burden for incumbents than is currently the case under present law and with a net decrease in the efficiency and effectiveness of the process.

Senator INOUYE. That would make it less flexible.

Thank you very much. Thank you, sir.

Senator KASSEBAUM. Do you have any questions, Senator Ford?

Senator FORD. Mr. Shane, what is the procedure of an airline today wanting to maybe get rid of a route? How do you give up a route? Do you just give it up or do you sell it off, or what do you do?

Mr. SHANE. The airline would in most cases give notice to the Department of Transportation that it intended to suspend service on an international route. If that were a route in which there were no governmentally imposed constraints on the number of airlines, it would simply drop out of the market. The U.S. Government would not take any particular action, because by its very nature the route was an open entry route. Presumably everybody that wants to serve is already serving. Anyone that wanted to come in and serve in light of the dropout would have an opportunity to come in and get designated. There would not be any trouble with the foreign government in our doing that.

On a limited designation route, where we only have authority to provide one or two or three airlines, the announcement by one of the incumbents that it intended to drop out would of course create an opportunity for a replacement. And the Department of Transportation, upon learning of the intention of the incumbent to drop out of the market, would then commence a carrier selection proceeding to find a replacement for that carrier.

Once we selected a replacement carrier, we would simply notify the foreign government in question that the designation of the incumbent that has left was being withdrawn and a new designation was being filed, that is to say for the newly selected carrier.

Senator FORD. Is that the only procedure of giving up a route? A route cannot be transferred to another airline for a price?

Mr. SHANE. Well, no, I was not saying that was the only procedure. And indeed, of course we have a proposal right now pending before the Department of Transportation, a proposal which I really can't comment on in any substance, in which Pan American and United propose a transfer of Pan American's International Pacific Division to United Airlines, including both facilities on the ground and aircraft and routes.

That is a proposal we are looking at. We have had similar proposals in the past. The Civil Aeronautics Board of course dealt with a proposal by Braniff to transfer all of its South American route authority at one point to Pan American. I believe in that case it ended up having a carrier selection proceeding and allocating that route authority through a more traditional process.

So there are a variety of options available to carriers. They all have to be reviewed by the appropriate regulatory authority—now it is the Department of Transportation—before being approved.

Senator FORD. So regardless of what I wanted to do, you would ultimately have the approval of any transfer of routes.

The United-Pan Am is basically a merger, is it not? They are just taking it over completely for a price?

Mr. SHANE. That is the nature of the proposal, yes.

Senator FORD. Why could that not be done by another airline? There is nothing to prevent that?

Mr. SHANE. Are you suggesting another airline could simply take its international route authority and sell it?

Senator FORD. Yes.

Mr. SHANE. Well, it could propose that kind of a sale. There have been route transfers in the past. The Civil Aeronautics Board dealt with a number of them and I believe they have been approved. But I believe that we would have to look at the circumstances of each proposed transfer and determine whether or not it was in the public interest or whether a more traditional carrier selection proceeding open to all comers would be the more appropriate way to go in the public interest.

Senator FORD. Well, even though I want to sell a route to you and we agree upon that for a given figure, then the Department of Transportation would ultimately have to make the decision to approve or disapprove. If they disapprove the sale, then the Department of Transportation would exercise its authority under present law for the traditional method of a selection by the Department of Transportation of getting out of that international route.

What if I wanted to sell it to you and the Department says, no, we want to go the more traditional route? Then can I withdraw that sale?

Mr. SHANE. Yes. To the extent that there has been no consummated transaction, you would still be the incumbent on the route. You would still have a certificate to provide service, and it would be your option to provide that service, subject only to possible challenges from other aspiring entrants or to the expiration date in your certificate.

Senator FORD. Thank you, Madam Chairman.

Senator KASSEBAUM. Senator Inouye.

Senator INOUYE. Just one question, and it may not relate directly to the matter at hand. On these routes where you have permanent authority and temporary certificates, is it correct that all of the foreign carriers operate under permanent authority?

Mr. SHANE. I am not fully briefed on the nature of the authority that all foreign carriers operate under, Senator. But my guess is that that is a correct statement.

Senator INOUYE. Is it also correct that none of the American carriers are owned by the Government?

Mr. SHANE. Yes.

Senator INOUYE. Wholly or partially?

Mr. SHANE. The U.S. Government does not own any commercial air carriers, no, sir.

Senator INOUYE. Is it not also correct that all other foreign airlines are owned, either in whole or in part, by foreign governments?

Mr. SHANE. No, sir, I do not believe that is the case.

Senator INOUYE. What about British Airlines and Air France, Saudi Arabia, El Al?

Mr. SHANE. There are certainly many examples of foreign airlines which have some ownership vested in the foreign government in question. But that is by no means a universal phenomenon. In the case of the United Kingdom, British Airways is partially owned by the Government of the United Kingdom. That is ownership which the United Kingdom is trying mightily to divest itself of at the moment, so you would not have an example of that phenomenon in the United Kingdom once that privatization is complete.

There are a variety of other carriers in the United Kingdom which are not governmentally owned. Similarly, there are private airlines in many other European countries which have no Government ownership, as well as in other parts of the world.

Senator INOUYE. But is it not correct to characterize that the major foreign airlines have some Government involvement?

Mr. SHANE. It is certainly not an unusual phenomenon, no.

Senator INOUYE. Thank you very much.

Senator KASSEBAUM. Mr. Shane, to what degree are carriers free to change the service or fare level on routes that they hold certificates for?

Mr. SHANE. Madam Chairman, if they have a temporary experimental certificate based upon their proposal to provide innovative low-cost service in a market, probably in a new market, then any dramatic change from the proposal would open the carrier to at least the risk that someone else would come in and make a proposal that seemed more attractive in terms of the public interest than what the incumbent was in fact doing in the market.

So under those circumstances, there might be somewhat less flexibility for the incumbent to alter its proposal. In fact, the law is designed to ensure that the incumbent does not change its proposal dramatically and that it continues to provide the kind of service which the selecting authority, the Department of Transportation now, expected it to provide.

If in fact a particular approach to a market simply does not work as a practical matter and the carrier is unable to operate successfully on the basis of its proposal, well, as a regulatory authority we would want to know what its reasons were for making the changes it made and examine those reasons and examine the marketplace to the greatest possible extent and recognize the need for flexibility.

It may require an approach that was difficult to formulate on the basis of an abstract guess about the nature of the market during the carrier selection proceeding. What I am saying, Madam Chairman, is that we would try to be reasonably flexible in giving carriers, particularly carriers in limited entry markets, a reasonable amount of leeway to try to exploit those markets in the most effective possible way, with the bottom line consideration always in mind that we are basically in business to make sure that the public gets the kind of service it deserves.

Senator KASSEBAUM. I am just curious. If you have a temporary certificate in a limited market, I assume that market could become an unlimited market at some point in a bilateral agreement. Has that occurred?

Mr. SHANE. It could occur and I suspect it has occurred, yes. I know it has occurred.

Senator KASSEBAUM. At that point, what happens to the temporary certificates? Do they become automatic permanent ones or is there a whole proceeding or competition they all have to go through?

Mr. SHANE. If a market that had been constrained by a bilateral agreement suddenly became unconstrained by virtue of an amended bilateral agreement, then as a practical matter, even though there was an expiration date in the incumbent's certificate by virtue of its having been granted under constrained circumstances, there would be, I suspect, an automatic extension of that certificate.

There would be no purpose in having a renewal proceeding if the market had by that time become an open market.

Senator KASSEBAUM. Have any of the temporary certificates under consideration here actually gone through the review process?

Mr. SHANE. No. Well, let me correct myself. We asked the CAB, as I indicated in my opening statement, to postpone the renewal dates on most of the certificates that were coming up for renewal right about the time of sunset or within a few months afterward, simply because we felt that if they didn't then the CAB would have to commence proceedings that it could not complete and that would be unfair to litigants. Litigants would have no idea what decisional criteria the Department of Transportation might apply to cases that had been commenced in a different agency and so forth.

The CAB recognized the soundness of that approach and did in fact postpone almost all of the cases. We had three proceedings which involved authority that was not being used by U.S. carriers and which we felt ought not to be postponed because the public interest simply warranted that that service be introduced as quickly as possible. That was the Miami-London case, the Houston-London case, and the Tampa-Yucatan case.

Senator KASSEBAUM. And in all of those cases, the carrier changed, I assume, because the original was not being used, is that correct?

Mr. SHANE. Well, in the case of Miami-London Air Florida had been the incumbent, and of course they dropped out of the market upon filing for bankruptcy.

Pan American had not been serving in the Houston-London case because it had not entered the market at the one time it could have entered in order to provide the service on a continuing basis. So by the time we looked at the market, it was precluded from serving by virtue of the bilateral agreement. And as I indicated earlier, after the carrier selection process was completed we ended up awarding the route to Continental.

Tampa-Yucatan was not a replacement case. We were simply awarding authority to a new carrier, if I'm not mistaken.

Senator KASSEBAUM. You mentioned that you had announced last year that there would be a proposed rulemaking procedure.

Mr. SHANE. Yes.

Senator KASSEBAUM. When last year was this announced? I'm just curious. When now—do you have a definite date by which you're going to do this?

Mr. SHANE. I testified last year in the spring and promised that we would have the rulemaking out in the first half of the year. I have virtually a final draft of the notice of proposed rulemaking in my briefcase right now. We had anticipated getting it out a little earlier, but the unexpected arrival of three major route cases at the Department of Transportation during this first 6-month period, at a time when we did not expect to be dealing with anything, I think necessitated a slowing down of that schedule.

I don't have a definite date, Madam Chairman, but I would expect that it would be out within the month. We are required under the administration's procedures, of course, to submit our proposed draft to the Office of Management and Budget for its review, but my expectation is that we will not have a very long time to wait before we get it cleared.

Senator KASSEBAUM. You will make these—you have three cases pending for temporary renewal?

Mr. SHANE. No. Those three cases are now completed. There are some procedural opportunities for petitions for reconsideration and so forth, but in terms of the Department's principal effort we are past those three cases at this stage.

Senator KASSEBAUM. Any further questions?

[No response.]

Senator KASSEBAUM. Thank you, Mr. Shane.

Mr. SHANE. Thank you very much.

[The following information was subsequently received for the record:]

QUESTIONS OF SENATOR HOLLINGS AND THE ANSWERS

Question 1. You have stated that the Department is expected to begin a rulemaking on the duration of international airline certificates. Can you be more specific as to when the notice of proposed rulemaking will be issued? Can you tell the Committee precisely where this proposed rule is at this point in time in the internal administration review process?

Answer. While I cannot provide an exact date on which the Department's notice of proposed rulemaking will issue, I can tell you that the rulemaking draft is undergoing the final stages of review within the Department. Although it must be reviewed by the Office of Management and Budget prior to its publication in the Federal Register, it is our objective to issue a notice of proposed rulemaking in the near future.

Question 2. Following the issuance of this NPRM, does the Department envision pursuing this rulemaking to its completion, or is this simply a means of collecting data and forestalling legislation?

Answer. I can assure the Subcommittee that the Department of Transportation is fully committed to pursuing this rulemaking to its conclusion. The collection of data through the solicitation of public comments is not an end in itself, but a means to enable the Department to adopt a final rule which is responsive to the needs of both the industry and the traveling public.

Question 3. How many certificates are we talking about revising under S. 586? If you cannot be precise for us today, what is a good guess of the number of temporary international certificates now held by U.S. carriers—10, 25, 50, 100? How many have been subject to challenge during the individual certificate renewal proceedings?

Answer. There are approximately 55 temporary certificates (either in whole or in part) held by U.S. carriers.

During the past five years, there were at least three certificate renewal cases that were contested for various reasons, and two of those cases involved formal oral evidentiary hearing procedures. The three contested renewal cases involved the following routes and incumbent carriers:

Spokane-Vancouver (Frontier).
Houston-Yucatan (Texas International)[1]
Houston-London (Pan American).[1]

Question 4. Please provide for the record a listing of both indefinite and temporary/experimental internatioanl certificates now held by U.S. carriers in each foreign market.

Answer. Prior to 1978, the Civil Aeronautics Board issued both permanent/indefinite and temporary certificates for authority in international markets. The vast majority of these certificates were permanent/indefinite. After enactment of the Airline Deregulation Act of 1978 (ADA), the Board undertook a policy of awarding permanent/indefinite authority only in multiple permissive entry markets. Temporary and experimental certificates were issued in all markets where entry was restricted.

Therefore, we have answered this question in three parts. Part I summarizes temporary and experimental certificates currently in effect, showing the certificate holder and the current expiration date. Part II summarizes the permanent or indefinite certificate authority in multiple entry markets granted since the ADA showing, by foreign country, the number of carriers granted scheduled combination (passengers, property and mail) authority and all cargo route authority. Part III shows permanent scheduled route authority, by carrier, in limited-entry international markets issued during the period 1938 to 1978.

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[1] Formal hearing procedures were used to resolve the issues in these cases.

PART I.—TEMPORARY/EXPERIMENTAL CERTIFICATES BY CARRIER AND MARKETS

Carrier	Market	Certificate expiration date
Delta	Atlanta-London	Mar. 26, 1986
Northwest	11 U.S. Points-Scotland	Mar. 26, 1986
TWA	12 U.S. Points-London and Mendenhall England; Ireland (except Shannon); France (except Paris); Greece (except Athens); Israel (except Tel Aviv); Italy (except Rome); Iraq; Saudi Arabia; Yemen; Burma; and Vietnam.	Mar. 26, 1986
TWA	12 U.S. Points-The Azores; Portugal; Italy; Spain; Algeria; Tunisia; and Libya	Mar. 26, 1986
Pan American	16 U.S. Points-Barcelona; Nice; and Rome	Mar. 26, 1986
Pan American	San Juan-The Azores; Lisbon; Madrid; and Rome	Mar. 26, 1986
Pan American	11 U.S. Points-Ireland (except Shannon); United Kingdom; Paris; East Germany; Poland; Leningrad and Moscow; Czechoslovakia; Austria; Hungary; Rome; Yugoslavia; Romania; Bulgaria; Turkey; Lebanon; Syria; Iraq; Iran; Afghanistan; and Pakistan.	Mar. 26, 1986
Pan American	New Orleans/Tampa/Miami-London and Paris	Mar. 26, 1986
Pan American	New York/Boston-Madrid; Casablanca	Mar. 26, 1986
Northwest	Minneapolis/St. Paul-London	Mar. 26, 1986
Northwest	Boston-London	Mar. 26, 1986
World	Baltimore-London	Apr. 1, 1986
American	Dallas/Ft. Worth-5 Western Mexico Points	Apr. 21, 1986
Continental	Houston-8 Western Mexico Points	Apr. 21, 1986
Eastern	Atlanta/New Orleans-6 Western Mexico Points	Apr. 21, 1986
Pan American	Miami/Tampa-Mexico City	Apr. 26, 1986
Frontier	Alburquerque/El Paso-12 Western Mexico Points	May 8, 1986
Republic	Detroit-Montreal	May 14, 1986
US Air	Cleveland-Toronto/Montreal	May 14, 1986
Airlift	Miami/Houston/Puerto Rico-9 Latin American Countries (All-Cargo Service)	June 6, 1986
Republic	Chicago-6 Western Mexico Points	June 10, 1986
Pan American	Miami-London	June 18, 1986
Western	Anchorage-London	July 29, 1986
Eastern	Atlanta-Yucatan, Mexico	Sept. 11, 1986
Eastern	Miami-Merida, Mexico	Sept. 11, 1986
Western	Los Angeles-4 Western Mexico Points	Sept. 21, 1986
Arrow	Denver-London	Sept. 30, 1986
American	Cleveland-Yucatan, Mexico	Oct. 1, 1986
Eastern	Miami-Cancun/Cozumel, Mexico	Oct. 1, 1986
Evergreen	Detroit-Yucatan, Mexico	Oct. 1, 1986
United	Chicago/New York-Yucatan, Mexico	Oct. 1, 1986
Frontier	Spokane-Vancouver	Nov. 16, 1986
Capitol	San Juan-Brasilia and Rio de Janeiro, Brazil	Nov. 22, 1986
Eastern	New Orleans-Yucatan, Mexico	Dec. 5, 1986
Pilgrim	New York-Ottawa, Canada	Dec. 28, 1986
American	Houston/Dallas—Ft. Worth-Toronto/Montreal	Dec. 28, 1986
Continental	Houston-Yucatan, Mexico	Jan. 10, 1987
American	Dallas/Ft. Worth-Yucatan, Mexico	Jan. 10, 1987
Pan American	New York/Boston-Kenya	Feb. 11, 1987
Pan American	New York/Boston-Ivory Coast	Mar. 28, 1987
Pan American	Los Angeles/San Francisco/New York/Honolulu-Beiging and Shanghai, Peoples Republic of China.	Feb. 13, 1988
Flying Tiger	United States-Japan (All-Cargo)	Feb. 13, 1988
American	Dallas/Ft. Worth-London	Mar. 8, 1988
Continental	Houston-Acapulco	Mar. 8, 1988
Northwest	Chicago/Los Angeles/San Francisco/Honolulu/Seattle-Shanghai, Beijing and Guangzhou, Peoples Republic of China.	Apr. 7, 1988
Continental	Houston/Dallas-Ft. Worth/New Orleans-Caracas and Maracaibo, Venezuela	Apr. 8, 1988
Eastern	Various U.S. Points-several countries in South America (formerly Braniff routes)	Apr. 27, 1988
People Express	Newark-London	May 11, 1988

PART I.—TEMPORARY/EXPERIMENTAL CERTIFICATES BY CARRIER AND MARKETS—Continued

Carrier	Market	Certificate expiration date
Arrow	Tampa-London	June 17, 1988
Air Florida	Miami-Madrid/Tel Aviv	Aug. 29, 1988
Arrow	Denver-London	Sept. 30, 1988
Western	Los Angeles-Calgary/Edmonton	Oct. 12, 1988
United	San Francisco-Calgary/Edmonton	Oct. 12, 1988
Capitol	Los Angeles-Toronto/Montreal	Feb. 22, 1989
America West	Las Vegas-Calgary/Edmonton	Sept. 7, 1989
Capitol	Los Angeles-Toronto/Montreal	Feb. 22, 1989
America West	Las Vegas-Calgary/Edmonton	Sept. 7, 1989
Flying Tiger	United States-Venezuela (All-Cargo)	Oct. 25, 1989
Northwest	London-Frankfurt (May 15-October 28 each year)	Oct. 28, 1989
World	London-Frankfurt (October 29-May 14 each year)	Oct. 28, 1989
Arrow	Puerto Rico-Venezuela	Dec. 5, 1989
Arrow	San Juan-Toronto/Montreal	Dec. 21, 1989
TWA	St. Louis-London	Jan. 23, 1990
Northwest	U.S. Points-Dublin	Jan. 23, 1990
Cascade	Spokane-Calgary/Edmonton	Jan. 23, 1990
Continental	Houston/Dallas-Ft. Worth/Anchorage/Fairbanks-Calgary and Edmonton	Feb. 5, 1990
Flying Tiger	United States-Vietnam (All-Cargo)	Feb. 13, 1990
Arrow	Tampa-Yucatan, Mexico	May 25, 1990
Continental	Houston-London	May 25, 1990
Eastern	Miami-London	June 23, 1990

Part II. U.S. Carriers Holding Indefinite Certificate Authority to Countries Allowing Permissive Entry (As of 6/1/85)

Since October 1978, U.S. carriers have received new or additional permanent authority to provide scheduled service on a multiple permissive entry basis between any U.S. city and 51 foreign countries:

11 European Countries, 8 Pacific Countries, 7 Middle East Countries, 7 Central American Countries, 15 Caribbean Countries, and 3 South American Countries.

Following is a list, by country, of the number of U.S. carriers holding indefinite certificate authority to provide scheduled service between any point in the United States and any point or points in the indicated foreign country.

NUMBER OF U.S. CARRIERS HOLDING INDEFINITE CERTIFICATE AUTHORITY BETWEEN THE UNITED STATES AND MULTIPLE PERMISSIVE ENTRY COUNTRIES (AS OF 6/1/85)

	Number of U.S. carriers		
	Combination authority	All-cargo authority	Total
Europe:			
Austria	4	2	6
Belgium	23	3	26
Denmark	3	2	5
Finland	4	0	4
France	7	5	12
Germany, West	24	2	26
Greece (Athens)	7	2	9
Ireland (Shannon)	11	4	15
Luxembourg	17	2	19
Netherlands	21	3	24
Switzerland	16	1	17

NUMBER OF U.S. CARRIERS HOLDING INDEFINITE CERTIFICATE AUTHORITY BETWEEN THE UNITED STATES AND MULTIPLE PERMISSIVE ENTRY COUNTRIES (AS OF 6/1/85)—Continued

	Number of U.S. carriers		
	Combination authority	All-cargo authority	Total
Pacific:			
Hong Kong	19	1	20
India	6	1	7
Indonesia	7	1	8
Korea	17	1	18
Malaysia	6	0	6
Singapore	15	1	16
Taiwan	18	1	19
Thailand	15	1	16
Middle East:			
Bahrain	4	3	7
Egypt	6	3	9
Israel (Tel Aviv)	14	2	16
Jordan	11	0	11
Kuwait	4	1	5
Lebanon	4	1	5
United Arab Emirates	4	5	9
Central America:			
Belize	15	1	16
Costa Rica	14	2	16
El Salvador	15	1	16
Guatemala	16	1	17
Honduras	16	1	17
Nicaragua	15	2	17
Panama	15	2	17
Caribbean:			
Bahamas	18	0	18
Barbados	15	1	16
Barbuda, BWI	7	0	7
Bermuda	14	0	14
Dominican Republic	15	1	16
Guadeloupe	13	0	13
Haiti	16	1	17
Jamaica	18	2	20
Martinique	13	0	13
Netherlands Antilles	17	2	19
Grenada	9	0	9
Antigua	12	0	12
St. Kitts	10	0	10
St. Lucia	6	0	6
Trinidad and Tobago	13	2	15
South America:			
Chile	10	1	11
Colombia	9	5	14
Guyana	4	0	4

PART III.—U.S. CARRIERS' PERMANENT SCHEDULED ROUTE AUTHORITY IN LIMITED-ENTRY FOREIGN MARKETS ISSUED PRIOR TO 1978

Carrier	Certificate		Initial authority		Markets	
	Route	Segment	Order	Date	U.S. points	Foreign points
Alaska Airlines	124F	1	E-26301	January 1968	Northway	Dawson Creek.
		2	E-26593	March 1968	Ketchikan	Prince Rupert.
American	7	1	3520	January 1945	Buffalo, Detroit	Windsor.
	56	2	1010	April 1941	Buffalo	Toronto.
			E-4833	November 1950	Newark, New York, Rochester, Syracuse, Scranton, Wilkes Barre	Toronto.
		3	E-24904	March 1967	Chicago	Toronto.
			76-11-32	January 1977	Chicago	Montreal.
Continental	171	3	77-6-171	June 1976	Saipan	Japan.
	176	1	77-7-89	July 1977	Honolulu, Los Angeles, Pago Pago	Australia, New Zealand.
Delta	27F	1	72-8-1	August 1972	Boston	Montreal.
		2	72-8-1	August 1972	Augusta, Bangor, Bar Harbor, Boston, Lewiston, Portland, Rockland, Waterville	Moncton.
	154	1	72-8-1	August 1972	Miami, Tampa	Montreal.
Eastern	71F	1	E-17617	October1961	Syracuse	Montreal, Ottawa.
	72F	1	E-17617	October 1961	New York, Newark	Montreal, Ottawa.
	131	1	4793	May 1946	New Orleans	Mexico City.
			E-22741	October 1965 [1]	Washington, DC	Mexico City.
		1	E-24033	August 1966	Washington, DC	Acapulco.
			71-4-160	May 1971	Atlanta, New Orleans	Mexico City, Acapulco.
	131	2	[1] E-22741	October 1965	New York	Mexico City.
			E-24033	August 1966	New York	Acapulco.
	148	1	E-17830	February 1962	Buffalo	Toronto.
Frontier	73F	1	75-3-46	May 1975	Bismark, Minot	Winnipeg.
Northwest Airlines	3F	1	5030	July 1946	Grand Forks	Winnipeg.
			74-10-75	October 1974	Grand Forks	Edmonton.
	129	1	[1] E-11647	August 1957	Anchorage, Portland, Seattle	Japan.
		1	[1] E-16286	January 1961	Anchorage, Portland, Seattle	Okinawa, Philippines.
		1&2	69-4-90	April 1969	Hilo, Honolulu, Long Beach, Los Angeles, Ontario, San Francisco, San Jose, Chicago, Cleveland, Detroit, Minneapolis, Newark, New York, Philadelphia, Washington, DC.	Japan, Okinawa, Philippines.
	140	2	E-16285	December 1960	Anchorage, Chicago, Minneapolis, New York	Edmonton.
		2	74-10-75	October 1974	Anchorage, Chicago, Minneapolis, New York	Winnipeg.
Pan American	130	1	78	August 1938	Guam, Honolulu, Midway Island, San Francisco, Wake Island	Philippines. [2]
		1	E-8929	February 1955	Los Angeles	Philippines.
		1	E-11648	August 1957	Los Angeles, San Francisco	Japan.

		1	[1] E-16286	January 1961	Guam, Honolulu, Midway Island, Wake Island	Japan.
		1	69-4-90	April 1969	Hilo, Newark, New York	Japan, Philippines.
		2	552	June 1940	Honolulu, Los Angeles, San Francisco	New Zealand.[3]
		2	E-867	October 1947	Honolulu, Los Angeles, San Francisco	Australia.[4]
		2&3	69-4-90	April 1969	Hilo, Newark, New York, Pago Pago	Australia, New Zealand.
	130	4	69-4-90	April 1969	Fairbanks	Japan.
		5	75-6-152	June 1975	Baltimore, Chicago, Dallas/Ft. Worth, Washington, DC	Australia, New Zealand.
	132	1	55	April 1939	New York	London.
	Part I		[1] 3791	January 1950	New York	Dublin.
		1&2	[1] E-23230	February 1966	Baltimore, Boston, Chicago, Detroit, Los Angeles, Newark, Philadelphia, Portland, San Francisco.	Dublin, London.
		1&2	78-1-118	January 1978	Oakland, San Jose	Dublin London.
	136	a	592	August 1938	Miami, San Juan, St. Thomas	Buenos Aires, Caracas, Rio de Janeiro, Sao Paulo.
		b	592	August 1938	Miami	Merida.
		e	5033	August 1946	Houston	Mexico City.
		1	E-1981	September 1948	St. Croix	Buenos Aires, Caracas, Rio de Janeiro, Sao Paulo.
		7	E-1981	September 1948	New York	Caracas.
		I&II	E-2892	July 1949	Houston, New Orleans, New York	Buenos Aires, Rio de Janeiro, Sao Paulo.
		I&II	E-2892	July 1949	Houston, Miami, New Orleans,	Maracaibo.
		I&II	E-25174	July 1967	Baltimore, Boston, Newark, Philadephia, Washington, DC	Buenos Aires, Caracas, Rio de Janeiro, Sao Paulo.
		IV	E-25174	July 1967	Miami	Mexico City.
	136	I&II	[1] 68-11-120	January 1969	Los Angeles, San Francisco	Buenos Aires, Caracas, Maracaibo, Rio de Janeiro, Sao Paulo.
		I	77-9-63	November 1977	Dallas/Ft. Worth	Buenos Aires, Caracas, Maracaibo, Merida, Rio de Janeiro, Sao Paulo.
		I	78-6-218	June 1978	Baltimore, Los Angeles, New York, Washington, DC	Mexico City.
Republic (formerly North Central)	86F	1	E-15741	May 1960	Duluth/Superior	Thunder Bay.
		2	E-24903	May 1967	Detroit	Toronto.
		3	[1] 78-4-45	June 1978	Duluth/Superior, Milwaukee	Winnipeg.

PART III.—U.S. CARRIERS' PERMANENT SCHEDULED ROUTE AUTHORITY IN LIMITED-ENTRY FOREIGN MARKETS ISSUED PRIOR TO 1978—Continued

Carrier	Certificate		Initial authority		Markets	
	Route	Segment	Order	Date	U.S. points	Foreign points
Texas International (d/b/a Continental).	86F	1	68-9-124	December 1968	McAllen	Monterrey.
		2	68-9-124	December 1968	Harlingen	Tampico, Veracruz.
		1	72-5-1	July 1972	McAllen	Mexico City.
		1	72-5-1	July 1972	Houston	Mexico City, Monterrey.
		1	78-6-198	June 1978	Houston, McAllen	Guadalajara.
Trans World	147	1	[1] E-6560	June 1952	New York	Rome.
		1	E-11567	July 1957	Los Angeles, San Francisco	Rome.
		1	[1] E-23230	April 1966	Baltimore, Boston, Chicago, Detroit, Philadelphia, Washington, DC	Rome.
		11	78-1-118	January 1978	Newark, Oakland, San Jose	Rome.
	164	1	69-4-90	May 1969	Hilo, Honolulu, Long Beach, Los Angeles, Ontario	Okinawa.[5]
US Air (formerly Alleghany)	97F	1	E-24903	May 1967	Erie	Toronto.
		2	72-4-52	April 1972	Buffalo	Toronto.
		1	75-1-22	January 1975	Buffalo, Rochester	Montreal.
	97F	2	75-8-24	September 1975	Rochester	Toronto.
		3	75-8-25	October 1975	Boston	Toronto.
United	57	1	57	August 1938	Seattle	Vancouver.
		2	E-24904	May 1967	Chicago	Toronto.
		1	78-1-65	March 1978	Chicago	Vancouver.
Western	52	1	796	December 1940	Great Falls	Lethbridge.
		1	5035	July 1946	Great Falls	Calgary, Edmonton.
		2	E-24902	May 1967	Los Angeles, Portland, San Francisco	Vancouver.
		1	68-9-146	November 1968	Denver	Calgary, Edmonton, Lethbridge.
		3	76-2-1	April 1976	Honolulu	Vancouver.
	152	1	4793	May 1946	Los Angeles	Mexico City.
		1	E-571	May 1947	San Diego	Mexico City.
		1	E-24033	September 1966	Los Angeles, San Diego	Acapulco.
		1	78-5-182	May 1978	San Francisco	Acapulco, Mexico City.
		1	78-5-182	May 1978	Los Angeles, San Diego, San Francisco	Guadalajara.

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[1] This order granted permanent authority where the authority was previously temporary.
[2] Pan American's Philippine service was limited to Manila service only.
[3] Pan American's New Zealand service was limited to Auckland service only.
[4] Pan American's Australia service was limited to Sydney and Melbourne service only.
[5] Trans World's authority over Pacific Route 164 was suspended for a year as part of a route agreement with Pan American. See Orders 77-1-7 and 78-3-8.

Question. 5. Apart from the merits of temporary v. permanent certificates, what is your view of the proposed bumping provision included in S. 586?

Answer. The Department believes that S. 586 could result in more challenges to incumbent carriers than presently occur under a system of temporary certificates. Because the principal issue would be the challenger's purported ability to provide a substantially improved combination of fares and service, S. 586 appears to place greater weight on new proposals—however untested—than on experience in the market. As such, because the burden on a challenger appears to be so small, the bill might well create greater uncertainty than exists under present law.

Furthermore, it is likely that such challenges might occur earlier than at the end of the term of a temporary experimental certificate. Under the present system of limited-duration certificates, the Department is reluctant to entertain challenges to an incumbent's authority—except in unusual circumstances such as the withdrawal of most service from a market—until that carrier has had sufficient opportuntiy to develop traffic on the route and to demonstrate its intention and ability to provide good service at reasonable fares.

The Department also believes that the exclusive focus of S. 586 on fares and service as criteria in "bumping" cases ignores the fact that the competitive structure of any given market can undergo substantial change over time. Such changes could undercut those structural considerations that might have been the basis for the initial award of certificate authority. Under the provisions of S. 586, however, the Department could not take changes in market structure into account when determining whether to initiate a bumping proceeding, or in deciding such a case.

The bill requires that an applicant be "qualified" in order to challenge an incumbent for international route authority. The term "qualified" is ambiguous: Does it constitute a standard different from the requirement that an applicant be "fit, willing, and able" pursuant to section 401 of the Federal Aviation Act?

Subsection (10)(B) of the proposed legislation would provide for the replacement of an incumbent carrier where the Secretary finds, inter alia, that "restrictions arising from the provisions of a bilateral air transport agreement . . . or otherwise imposed by a foreign country, preclude or make it impossible for the Secretary to authorize an additional carrier in a particular foreign air transportation market. . . ." There are many cases where the U.S. has a bilateral agreement which provides for unlimited designations but where, as a practical matter, the foreign government has imposed a de facto limitation on the number of U.S. carriers that it will authorize to serve the market. In such instances, it has been our policy to seek the removal of these restrictions through negotiations. A public finding by the Secretary that restrictions, in direct contravention of the provisions of a bilateral agreement, preclude the designation of additional U.S.-flag service would undermine our position at the bargaining table. Furthermore, any such finding might well be seen by other governments as a sign that the U.S. is willing to acquiesce in further restrictions to entry on international routes. As a practical matter, therefore, it is highly unlikely that any such finding would ever be made.

Although not directly related to the bumping provision, another area of S. 586 causes us concern. In addition to restricting certificate authority in limited-designation markets to five years, the Board also limited some air carrier authority in order to facilitate further review of certain questionable aspects of that carrier's fitness. Because that section of the bill which would transform current temporary certificates into indefinite authority applies to any certificate to engage in foreign air transportation issued prior to the date of enactment, the bill would also encompass those certificates which were granted for a fixed term solely for reasons dealing with fitness. As a result, such certificates would be extended indefinitely, thereby eliminating the automatic fitness review which the Board sought to impose.

Question 6. To the best of your knowledge, why did the Civil Aeronautics Board begin issuing temporary certificates for international service? Secondly, why are some markets served under both permanent and termporary certificates?

Answer. The Civil Aeronautics Board awarded temporary certificates throughout its existence (1938–1984) when it found that political or economic conditions were such that it needed to retain flexibility to adjust operations to changing conditions. Prior to deregulation, the CAB frequently granted permanent awards when it was persuaded that a market would clearly "continue to occupy a major position" in the U.S. international route pattern. Some examples of this would include the New York-London and New York-Paris markets and the West Coast-Tokyo markets.

After deregulation, the CAB followed a policy of granting permanent authority in international markets where bilateral agreements permit unlimited entry of U.S. carriers. Temporary authority was awarded in markets where such agreements limit entry, primarily in accordance with the Board's policy of simulating competitive forces in monopoly markets through a periodic renewal process. Since 1978, the U.S. has introduced new carriers—by awarding them temporary experimental certificates—to a number of "major" markets that, while characterized by entry restrictions, were previously the subject of permanent awards. Thus, there are routes today that are served under both permanent and temporary certificate~~.

Question 7. Opponents to S. 586 argue that these international routes are "a public resource negotiated for the benefit of the nation as a whole, not inidividual airlines." What is the Department's response to this type of assertion?

Answer. We agree.

We assume that the opponent's underlying argument is that the grant of permanent international route rights to U.S. airlines would result in the establishment of a "propoerty right" in such authority. We do not believe that, with adequate bumping procedures, this would necessarily be the case. Before reaching a final conclusion, however, the Department will issue shortly a notice of proposed rulemaking that will ask for public comment on issues such as certificates duration, and appropriate replacement procedures.

QUESTIONS OF SENATOR INOUYE AND THE ANSWERS

Question 1. Under the current system of awarding international route certificates, carriers holding temporary certificates must go through renewal proceedings periodically to retain their route authority. I understand that these proceedings can be very involved and time consuming, often encountering lengthy delays. Could you outline the steps involved in this process and the average period of time between the initiation of the case and the awarding of a certificate renewal and the cost to the government of this entire procedure?

Answer. The process and time involved in the renewal of temporary international certificate authority vary considerably from case to case, depending primarily on whether the renewal application is contested.

Contested applications for limited-entry routes can be relatively lengthy and complex, given the need to ensure that all applicants are accorded due process and the need to establish an adequate record. Oral hearings with trial-type procedures (including detailed exhibits and post-hearing briefs) are the norm.

Yet, despite the necessity of such procedures, these cases are not open-ended. Procedural schedules are fixed, and adhered to, with statuory deadlines clearly in mind. In the pre-deregulation period, where no statutory deadlines existed, international route proceedings often took years to complete. Based on the CAB's post-deregulation experience, and the Department's own experience, these carrier selection cases can how normally be completed in from six to eight months. Even greater expedition is possible where circumstance demand.

For uncontested applications, procedural delays can be avoided almost entirely. With these applications, the Department can use simplified procedures, such as show-cause orders, thereby processing the entire matter on the written record without resort to trial-type proceedings. Barring unusual circumstances, staff work can be completed in just one to three months, at greatly reduced cost. The Board's recent experience indicated that a substantial number of applications for renewal of international route authority were likely to be uncontested.

The Department believes that some of the contested renewal application cases which previously were set for oral evidentiary hearing can be better resolved through the use of "show cause" procedures. This approach would be similar to the procedures used by the Board in uncontested cases, except that a tentative finding would be made by the Department and a period for objections would be provided before the rendering of a final decision. The use of show-cause procedures would be best suited to cases involving relatively straightforward issues amenable to resolution without an extensive evidentiary record.

We describe in more detail below the steps invoved in both the oral evidentiary and non-oral application renewal procedures.

OUTLINE OF THE STEPS INVOLVED IN CERTIFICATE RENEWAL

1. Non-oral Procedures: The Public Proceedings Division of the Office of Aviation Operations reviews the application for completeness. By regulation, they must reach their determination within 21 days. If the application is incomplete, it is returned to the applicant for completion.

If the application is complete, the staff awaits the prescribed period for answers (28 days) and then drafts an order responding to the application for signature by the Assistant Secretary for Policy and International Affairs.

Where no complex or controversial issues are raised, the first order drafted may be the order finally disposing of the application. In the usual case, such an order will grant the application, since the two principal tests—(1) fitness of the applicant, and (2) public convenience and necessity—will have been satisfied (fitness satisfied based on officially noticeable data; public convenience and necessity satisfied based on the procompetitive provisions of the Federal Aviation Act, as well as settled deregulation era policies favoring the encouragement of new U.S carrier competitive opportunities).

Where the application raises complex issues, or where answers are received that generate controversy, the first order drafted generally will be a show-cause order. This allows for a full airing of the issues and for comment on the Department's initial position. Once comments are received and fully analyzed, the staff prepares a second and final order for issuance by the Assistant Secretary, disposing of the application.

In either case, the entire process is conducted through non-oral procedures.

Time involved: one to three months (not including the 60-day period for Presidential Review).

2. Hearing Cases: The Department, through the Assistant Secretary for Policy and International Affairs, issues an order, instituting a route proceeding. This order establishes the scope of the issues to be decided, the procedures to be used, and the decisional criteria.

At the prehearing stage parties, including the DOT office serving as public counsel, file direct and rebuttal exhibits. The Administrative Law Judge holds a prehearing conference to discuss the evidence requests and to establish procedural dates.

An oral hearing is held at which all parties are allowed to present their evidentiary case. Parties also have the opportunity, at this stage, to cross-examine witness through testimony.

After receiving briefs from the parties, the judge evaluates the evidence and prepares a recommended decision addressing the issues in the case.

Parties (including public counsel) seeking review of the judge's Recommended Decision may file exceptions with the Department and all parties may then file briefs. The first level of review is with the Department's designated Senior Career Official. His decision can in turn be reviewed by the Assistant Secretary for Policy and International Affairs, or by the Secretary of Transportation. The Federal Aviation Act specifies that the Department has up to 90 days from the Recommended Decision to reach its final decision.

Based on his review of the record, Recommended Decision, and briefs which have been filed by the parties, the Senior Career Official may decide to hold an oral argument.

The Senior Career Official's staff prepares a memorandum of issues. This document summarizes the record and arguments of the parties (including public counsel), identifies the issues to be decided, and suggests useful areas for inquiry.

After time for deliberation, the Senior Career Official prepares an order reviewing the Recommended Decision.

That order is transmitted, confidentially, to the Assistant Secretary for Policy and International Affairs (or, where appropriate, to the Secretary) for review. The Assistant Secretary has 14 days to reach a decision on how to proceed.

The Assistant Secretary and his staff review the Senior Career Official's opinion. Based on this review, the Assistant Secretary can decide to return the opinion for modification, allow the opinion to take effect as a final order of the Department, or announce further procedures pursuant to his reaching a determination on how best to proceed.

Once the Assistant Secretary determines that an opinion can serve as a decision of the Department, it is transmitted to the President for his review under section 801 of the Act. If the President does not veto that opinion within 60 days, it is issued as a final Departmental order. Parties may petition for reconsideration with ten days of the date that the final order is issued.

Time involved: normally six to eight months (not including the time for the presidential review, or possible challenges subsequent to issuance of the Department's decision), but procedures have been expedited where circumstances demand.

COSTS OF RENEWAL CASES TO THE U.S. GOVERNMENT

Because procedures differ so much in terms of both time and resources, the cost to the government depends on a number of factors. These include the question of whether or not an application is contested, whether the case involves an oral evidentiary hearing or a non-oral "paper" proceeding, the number of parties contesting the renewal application, and the complexity of the issues which must be decided.

We have estimated that an average proceeding in which the application is not contested would cost approximately $1,000.

If the application is contested, but "show cause" procedures can be used instead of a full oral evidentiary hearing, the average cost is about $1,500.

A full oral evidentiary hearing costs the government approximately $39,000 to conduct.

It should be noted that these are estimates and that any particular case might exceed or fall below these figures. Also, these estimates only reflect the direct costs incurred by the Department of Transportation and do not include the costs to other agencies involved in the section 801 review process.

Question 2. To your knowledge, has a carrier ever been removed from a route as a result of these renewal proceedings? If so, could you explain the circumstances?

Answer. Some carriers have been removed from limited-entry routes where it appeared that another carrier could provide better public service. In the 1978 Transatlantic case, the Civil Aeronautics Board suspended Pan Am's authority to serve Scotland and Scandinavia and awarded it to Northwest. The CAB's basis for doing so was that Pan Am had suspended service to those areas; moreover, the U.S.-carrier share of the U.S.-Scandinavia traffic, which had never exceeded 13.3 percent, had dropped to less than 3 percent. (Docket 25908.)

In 1980, Texas International's temporary Houston-Yucatan authority was not renewed, and the authority was given to Continental. In that case, the CAB found that Texas International had increased its fares substantially over those it had proposed in order to get the award, and that its overall performance should give it no advantage over other applicants. It then determined that Continental, because of its ability to feed on-line traffic from other U.S. cities through Houston and its low-fare proposal, would benefit more travelers than would Texas International. (Docket 33220.)

In addition, Braniff's authority for the Dallas/Ft. Worth-London route in 1983 and Pan Am's authority for the Houston-London route 1985 were not renewed since those carriers had suspended service over the routes. (Dockets 40827 and 42603, respectively.)

Since deregulation, few renewal cases have been necessary because most temporary international authority was extended in 1982 for two years by Congress and, in 1984, by the CAB for a transition period at its sunset.

Senator **Kassebaum**. The next witness is Ed Meyer, chief executive officer, TWA.

It is a pleasure to welcome you this morning, Mr. Meyer. I would guess that at this point perhaps the international route awards is not at the top of your worry list.

STATEMENT OF ED MEYER, CHIEF EXECUTIVE OFFICER, TWA; ACCOMPANIED BY JOHN F. ASH, VICE PRESIDENT

Mr. **Meyer**. No, Senator, it is not. Shall I commence?

Senator **Kassebaum**. Please do.

Mr. **Meyer**. Madam Chairman, members of the committee, I am Ed Meyer, president and chief executive officer of TWA. My statement reflects the views of Delta, Eastern, Northwest, Pan American, United and TWA. With me is John F. Ash, vice president of TWA.

I am here to present our views on S. 586, a bill designed to amend section 401 of the Federal Aviation Act in order to make international route certificates indefinite in duration.

As you know, we are major U.S. carriers that operate the vast majority of the U.S.-foreign air transportation system. Consequently, we are extremely concerned that one of the more blatant, heavy-handed regulatory vehicles has not been sunset with the Civil Aeronautics Board; that is, the authority for the Department of Transportation to award some international route certificates on a periodic or term basis.

In our view, the route renewal process does not enhance competition but merely ensures that the bureaucracy is self-perpetuating. It forces the regulatory body to undertake a route case proceeding with all of its costs and ramifications. It also serves as a disincentive to a U.S. carrier to fully invest in the route and related facilities if its future is open to question.

In short, this is a highly unproductive practice. It has never, to our knowledge, resulted in the removal of a carrier from an international route that it was actively operating. And it leaves us with an inconsistent network of conflicting types of certificates. As a result, we often spend more time and money competing with each other in Washington than we do competing with the foreign flag carriers in the marketplace.

There are a myriad of reasons why certificates should be of indefinite duration. First, route renewal cases are guaranteed to be productive for a limited segment of the population: economists and lawyers. The last transatlantic route renewal case lasted 2 1/2 years and cost TWA roughly a half a million dollars in legal fees alone.

The bottom line, after this lengthy examination of the U.S. international route system, was that no actively operating carrier lost its certificate. Moreover, to the best of our knowledge, as previously mentioned, no one has ever lost a route as a result of a challenge in a route renewal case.

Second, there are major inconsistencies in the existing international route authorities held by various U.S. carriers. For example, between the U.S. and Europe TWA has indefinite route authority to Paris and Rome and has temporary or term limited authority to London and Lisbon. On the other hand, Pan Am's authority to London and Lisbon is indefinite, but their authority to Paris and Rome is termed limited.

There are many other examples of similar conflicting patterns which reflect little or no logic, the point being under existing law, whether it be yesterday's CAB or today's DOT, if a major route renewal case involving a number of foreign points should be scheduled, one carrier will have to defend certain points while others will not be required to defend the same points. Accordingly, the existing certificate pattern is not only illogical, it is also inequitable in terms of the requirements to defend authority in a route renewal case.

Third, the foreign flag competitors of U.S. carriers never face a route renewal problem. Their authority tends to be permanent. Foreign governments realize that they have enough control over their carriers to ensure against abuse in the market. In fact, so do the Congress and the executive branch under the Federal Aviation Act.

In that regard and as a final argument in favor of international certificates of indefinite duration is the fact that the Federal Aviation Act as it would stand after certificates are made indefinite would still allow the Federal Government control over carrier performance on routes in foreign air transportation.

There are several vehicles for such control. One is the ability of the DOT upon petition or on its own initiative to suspend, modify or revoke certificates for noncompliance under 401(g) after hearing, if required. In addition, the regulatory agency must approve fares and rates in foreign air transportation, and it can suspend a fare or rate for up to a year pending determination of its lawfulness. This means that if a carrier is failing to meet its obligations, the DOT has ample power to deal with the situation when it arises. This is far more practical and less costly than going through the burdensome renewal drill at the inflexible command of the calendar, regardless of the service actually being provided.

The DOT can institute certificate suspension proceedings at any time during the effectiveness of the carrier's authority. Requiring it to do so based upon some arbitrary date is a redundant regulatory intrusion that adds nothing to this process except unnecessary waste and expense.

The skeptics of the proposed legislation seem to believe that making certificates valid for an indefinite period will in some fashion create a monopoly or otherwise limit competition in markets that are relatively restricted by virtue of the nature of the bilateral agreement.

In our view, the facts do not substantiate this claim. All of us from time to time have been prevented from entering a market because the foreign government involved would not accept the designation of another U.S. carrier. What we tend to do is look for different opportunities until entry is possible. In the interim, it is not the responsibility of the incumbent carrier to get out of the market to make room for another airline. It is that second carrier's responsibility to either use its equipment in a different fashion or press the United States Government to secure additional operating rights so that it may enter the market.

When carriers want to offer new services, they have options for entry. For example, People Express was able to begin low fare service between Newark, NJ and London, England because of a right secured for it by the U.S. Government. That service is not available because another carrier was removed.

The opponents of indefinite certificates frequently attempt to sell the have versus have not argument. However, during the 4 or 5 years prior to its sunsent, the Civil Aeronautics Board handed out large numbers of route certificates to carriers which have ultimately not operated those routes. In some cases the carriers have even been designated and have operated for periods of 6 months to a year and then ceased operations. Consequently, to remove a carrier that has been operating for 30 years in order to inject a carrier which may or may not provide consistent service over the long term is a questionable proposition at best.

Moreover, there is a provision under section 401(g) of the act to revoke the authority of a carrier that fails to provide service for 90 consecutive days. There are markets where competition is very structured and where additional carriers, particularly those with extremely low costs might in theory provide consumer benefits. The problem, however, is that unless the foreign government is willing to accept the designation of that carrier at the carrier's price level, there is little to be gained by a replacement of one carrier with another through a route proceeding. In fact, if anything, the majority of the foreign flag competitors would be pleased to see a large, established U.S. carrier replaced by a small, new entrant.

A route renewal proceeding does not, contrary to popular assertions, stimulate competition. These cases merely address the replacement question and not the question how can we add more carriers or increase service levels.

In summary, we strongly urge passage of S. 586. If enacted, it will eliminate excessive and burdensome Government regulations and will save U.S. carriers from costly and nonproductive quasi-judicial proceedings.

That concludes our statement, and I will be happy to answer any questions.

Senator KASSEBAUM. Thank you very much. It is a pleasure to welcome the chairman of the committee, Senator Danforth. Do you have any comments you would like to make?

The CHAIRMAN. Madam Chairman, thank you very much.

I know, Mr. Meyer, that you are here for a particular purpose, and you are testifying not only on your own behalf and on behalf of TWA but also several other airlines. I would like, with your permission and with the permission of the chairman, to ask you some questions relating to the present situation of TWA and the efforts to gain control of TWA by Mr. Carl Icahn.

Mr. MEYER. Yes, Senator.

The CHAIRMAN. We in the Commerce Committee have jurisdiction over matters relating to air transportation. Heretofore, our concern, Congress' concern, has not been so much the ownership of any company, any corporation or any airline, but rather the question of the adequacy of air transportation and safety.

Would you explain to the committee any concerns that you might have with respect to the future of TWA?

Mr. MEYER. Yes, Senator. We have filed a petition for examination of the continuing fitness of TWA if Carl Icahn takes control of this airline. We believe on the basis of his compliance history, his inability and lack of experience in management or technical competence in the airline industry, and his lack of any creditable plan as communicated to me, that he would represent a threat in the operation of this airline.

We believe that this history is well documented by what he has done in other companies, and I would be happy to—I would like to submit it for the record. We have that petition before the Civil Aeronautics Board, answers to—excuse me, to the Department of Transportations. The answers are due next Monday, the 28th. And we hope or we urgently would hope that that would be set down for oral evidentiary hearing.

In the meantime, Mr. Icahn's activities are directed toward taking as immediate control of the company as he possibly can. I urgently believe that his control would be inimicable to our company and to the communities we serve and to the 10,000 employees who live in Missouri and Kansas, to the 20 foreign countries which we serve and the 17,000 other employees of the company, and that we need to hold everything still to prevent that control from changing hands until the oral evidentiary hearing is held by the

Department of Transportation, and they are allowed to reach a conclusion and a finding.

The CHAIRMAN. You have had discussions with Mr. Icahn?

Mr. MEYER. I have had several discussions, Senator.

The CHAIRMAN. What has he said to you about the future of TWA as an operating airline?

Mr. MEYER. Those conversations, which have been extensive, began with him proposing that a leverage buyout of the company could be done, and that it would cost $700 million, and that after all, the management of the company could easily shoulder the burden of $100 to $125 million of interest.

He proceeded to then propose that we could ground aircraft and routes not associated directly with St. Louis and with the international complexes we operate and raise $600 million, getting rid of airplanes and employees. His perception is that we are a cash-rich company. He absolutely stonewalls the fact that we need to spend money even on let alone new equipment, on the continuing operations to maintain the airline, our terminals and other facilities.

I find nothing he has suggested or talked to me about as being responsible.

The CHAIRMAN. Has he not indicated in his recent conversations that he intends to continue to operate TWA pretty much as is?

Mr. MEYER. I see nothing in this man's record that would give me any confidence in what he would either say or write.

The CHAIRMAN. Why?

Mr. MEYER. Would you like me to read what has happened in the past, and which I would submit for the record?

Phillips Petroleum, Phillips tripled its debt as a result of a restructuring plan underlying its agreement with Icahn to end his hostile takeover attempt. The company plans to sell off $2 billion in assets to help pay for stock repurchase.

Chesborough-Ponds, Chesborough-Ponds forced to buy ACF Polymer Corp. for $95 million. In addition to repurchasing Icahn's stak to finance purchase, the company went into debt.

Tappan Industry, Tappan was sold by its chairman, W.R. Tappan, to AB Electrolux as a defense against Icahn's plans to liquidate the company. Icahn had previously been put on the company's board after purchasing a 5 percent stake.

Marshall Field Co. agreed to be taken over by Batus, Inc. during the course of a fight with Icahn.

Dan River Co. Dan River went private, and an employee buyout as a result of fight with Icahn. Since 1983 the company has closed four plants, sold another, and laid off about 1,000 hourly workers. All together, company employment has shrunk to about 8,000 from 12,000.

Questions have risen over merits of an ESOP which replaced company pension plan. Much friction exists between management-employees, most of whom feel they got took by ESOP buyout.

ACF Industries, one of two companies actually acquired by Icahn. Since having been acquired, many units sold off or for sale. Company assets have been used as collateral to finance Icahn investments.

In 1984 ACF floated bond through Drexel Burnham to raise $400 million. Icahn replaced the existing independent trustee managing company's pension plan benefits with himself.

Saxon Industries, Saxon bought out Icahn's stake at a high premium, about 25 percent of the then-market value. Saxon entered into bankruptcy law proceedings in 1982 seeking protection from creditors while trying to work out a debt settlement.

Hammermill Paper, Hammermill bought out Icahn's stake at a premium after engaging in 14 months of heavy liquidation.

And there are a couple of others. And I have not cited his compliance record.

The CHAIRMAN. Meaning?

Mr. MEYER. With the regulatory administrative procedures of the Securities and Exchange Commission, the New York Stock Exchange, the State of Virginia, New Jersey and New York.

The CHAIRMAN. Your concern is therefore that he will do what with TWA?

Mr. MEYER. That he will take control of it and attempt over a period of time to liquidate it, or at the very least spend absolutely no money, which would thereby make it unable to compete in the very fiercely competitive domestic aviation market and result in a reduction of employment and the eventual, in my opinion from every suggestion he has made to me, the bankruptcy of the company.

The CHAIRMAN. How much stock does he own now?

Mr. MEYER. A little over 24 percent, I believe.

The CHAIRMAN. You have petitioned DOT to hold a fitness hearing; is that correct?

Mr. MEYER. Yes, sir.

The CHAIRMAN. And what has been the response to that request?

Mr. MEYER. They have set a date of the 28th of this month for responses.

The CHAIRMAN. Now, to what extent is time of the essence, in your opinion?

Mr. MEYER. At the present time we have a court proceeding in the southern district, and action is held in abeyance. If that action is removed——

The CHAIRMAN. Action of what sort?

Mr. MEYER. It's an action that he failed to disclose his complete intent in the section 13(d)'s that he has filed with the SEC.

The CHAIRMAN. But you said action is held in abeyance?

Mr. MEYER. His action is held in abeyance from taking control of the company until a further hearing before the judge takes place.

The CHAIRMAN. And that is scheduled when?

Mr. MEYER. For Friday morning.

The CHAIRMAN. For Friday morning?

Mr. MEYER. I believe.

The CHAIRMAN. So your concern is that after Friday morning and before sometime in the middle of next week something will happen?

Mr. MEYER. Something could very well happen. The middle of next week is only a schedule for a reply date. There are no hearings set down at this point in time, and that could take time, I think, as you know. And so therefore, what I think is urgently needed is a freeze on the situation as it now exists. After all, if Mr. Icahn's true intentions are as stated, he should have no problem with that proceeding.

The **Chairman**. Well, as you know, there has been a great deal of concern in Congress, as well as on your part, about the future of a major air carrier. As you point out, TWA is certainly a major—it certainly is major for my State and Senator Kassebaum's State. St. Louis is the hub city of your airline, and Kansas City is certainly a major center for your airline, as well as being the site of the overhaul base. And as you point out, there are some 10,000 TWA employees located in Missouri and in Kansas, many of them right on the border of Missouri and Kansas. This matter is under active consideration now in the Congress, and I think that it is fair to say that it is the strong feeling of everyone I have talked to that Congress, which has been attempting to get out of the business of regulating airlines now for the last number of years, would not stand by and simply see a major airline liquidated.

Now, what not standing by entails, what affirmative step that entails I think is something that we are going to have to review very carefully and very quickly. I do not know whether your fear is a well-founded fear or not. I mean that is your view. I am sure he would have another point of view to express to us. But the kind of fear that you express, namely that this is an acquisition either for the purpose of liquidation or for the purpose of letting TWA just wither away on the vine, that, as far as I am concerned, is something that Congress would not accept. Although the general concept of deregulation is one that I have supported, I would be in there feet first.

Thank you, Madam Chairman.

Senator **Kassebaum**. Thank you, Senator Danforth.

Senator Inouye, do you feel your questions may be anticlimactic?

Senator **Inouye**. Madam Chairman, I am certain you will recall I was one of the very few who opposed deregulation. I believe the minority statement which I issued suggested that these things could happen. However, that is history.

The central question on the TWA-Icahn matter has been asked by the chairman of this committee. I, too, am very much concerned with what is happening. If it were just a little airline that ran between two cities somewhere in middle America, it may be of concern to those two cities, but this is an airline that not only services the United States but vast portions of the world. We are talking about a major airline, as the distinguished chairman has pointed out.

Mr. Meyer, it is your contention that notwithstanding the communication that Mr. Icahn has sent to you, this letter to the board, that you have concerns, suspicions that Mr. Icahn will not in fact control and manage TWA and not dismantle it? It is your fear that it will be dismantled?

Mr. **Meyer**. Yes, it is, or it will not be properly operated. I have grave concerns about that on the basis of the many conversations I have had with him. And I would urge the Congress and the Senate to take immediate action to direct the Secretary of Transportation to freeze this situation until the proper hearings and conclusions can be reached. I believe it is urgent.

Senator INOUYE. This so-called freeze, what time frame are you talking about?

Mr. MEYER. Immediately. Today, if possible.

Senator INOUYE. Today. But for how long?

Mr. MEYER. I believe that legislation has been introduced in the House that would freeze it up to 90 days, and for whatever time it takes for the Department of Transportation to have its hearing and reach a conclusion.

Senator INOUYE. Madam Chairman, I have a whole set of questions relating to the real matter at hand that I would like to submit to Mr. Meyer, and it just relates to the number of renewal proceedings and cost of such proceedings and whether you have been challenged. And so if I may, I would like to submit those.

Senator KASSEBAUM. Without any objection, that will be done.

Senator Ford, do you have any observations?

Senator FORD. I do not know about observations.

Are the junk bonds involved in the sale or purchase of TWA, the so-called junk bonds?

Mr. MEYER. I believe it is possible part of the proceeds that are being used here have been raised through that route, yes, sir, with ACF Industries.

Senator FORD. We are talking about international routes now, and whether permanent or on a renewal period.

What authority then would the purchaser of TWA have as it relates to income if the purchaser attempted to sell off the so-called routes?

In listening to the Secretary a few moments ago, one, they would have to approve that sale. If they did not like it, they would come back and go through a normal route selection process.

So your concern is a takeover of the company, and our concern here today is the routes of—the international routes. So let's look at it on the basis of the sale of your international routes. What could benefit the purchaser from that under the statement given by the Department earlier?

Mr. MEYER. It does not seem to me that international routes are the property of the carriers to sell. They are the property of the Federal Government, and it seems to me that where the Government holds hearings to determine whether someone has the right to have that license to operate that route, that in the case particularly of a hostile takeover or the transfer of those rights, that it would only make sense that the Federal Government under the Department of Transportation have a right to examine and approve the award of that route. They are the property of the Federal Government.

Senator FORD. On takeovers, I am not sure, maybe you can tell me, how many takeovers are attempted on regulated industries? Are they all regulated that he has been after?

This is a severely regulated industry.

Mr. MEYER. This, to my knowledge, this is the first time a takeover, a so-called takeover has come to a regulated industry, certainly the airline industry.

The CHAIRMAN. CBS would be another one.

Mr. MEYER. It is my great concern, and you do normally raise the issue of fitness there with the operation of foreign routes, and I believe and am concerned that this will only lead to additional forays into the airline industry. After all, you have Pan American who, if that transaction is approved, will receive $750 million of cash.

Senator FORD. Pan Am will?

Mr. MEYER. That is the proposition.

Senator FORD. But that is a sale between airlines. That is not a takeover.

Mr. MEYER. No, no, but what I am saying is this is the first time someone has come at an airline, a regulated company. Of course, CBS is, I guess, another example of that, but my fear is, and patterns have been unfolding, of once they start on a company in an industry, they will go to other companies, that this will lead to the raiding or takeover of assets of other companies in the airline industry, and what I am saying is that if the transaction between United and Pan American is approved, Pan American will receive $750 million. And there is a preoccupation with companies that have cash or assets that can be liquidated.

Senator FORD. Well, as I understand it, the $750 million would be for the airplanes, the ground operation and all of that. You are really merging two airlines, or taking over, but your purchase is not necessarily just the designation for the airline. The $750 million would be used to acquire certain properties.

Mr. MEYER. United Air Lines would acquire routes which, as I say, are the property of the Federal Government, and they will acquire airplanes, and employees will be transferred, and facilities. That is what United receives. Pan American receives $750 million of cash and relief of certain obligations under leases as well, I believe.

Senator FORD. That is a little different than a hostile takeover, is it?

Mr. MEYER. No. But what I am saying is once the transaction is completed, then Pan American is an ideally profiled company for the takeover artists that exist in the United States and that prey on corporations who have assets that can be liquidated.

Senator FORD. When I was a small boy, I walked home late at night, and I had to go past a cemetary, and the later the night and the darker the moon, the more ghosts I saw behind the tombstones.

Now, you and I are talking about a sale between United and Pan American. But then you say that sale sets up—well, we have to go day by day, do we not, before we begin to look at a ghost behind the tombstone; that is, a ghost behind the tombstone as it relates to Pan American. You are using that to try to defend your position.

I am sympathetic, I think, with your position. I think the Department of Transportation ought to accelerate its review of the TWA situation. If they do not, I understand it is 28 percent now that Mr. Icahn owns, and that is better than the 24 percent, and he is moving pretty fast. If I know the bureaucrats around the Government, hell, he will have 51 percent before they read the testimony.

But what I am saying is that an accelerated review has to be done. However, I want to be careful that I look at your position and each other case on individual merits.

Mr. ASH. Senator, excuse me, if I might. This is not something that we have hypothesized. This is something that has been raised by the business press. The most recent Business Week article speculates that there is a perception that there is a great value in international routes, in particular, and that maybe airlines are "cash cows." And consequently, the Business Week article hypothesizes that this might be a next logical target industry, and that because of the history of the movement of takeover specialists from an industry to an industry.

Now, I do not think we have seen the press be terribly enthused about this industry because of the complexity and the questions of fitness and safety and the question of who owns those route rights. But they speculated; we did not.

Senator **Ford**. We had a fellow at home who was a sportswriter. You never heard of him, and he picked a long shot for the Derby. He has been a genius ever since.

But those who picked long shots and did not win, you have not heard of them. They do not have a syndicated column any more. So I guess you can speculate on what happens, and if it happens, they become the ones you want to look to. They make the fortune after that.

I can speculate on a lot of things, too, but I am not in that kind of business. I have got to try to protect and defend the future of a business. That is what I want to try to do, to try to help Senator Inouye with his legislation. I think it has some valuable assets.

I think we have strayed just a little bit from the intent of the legislation, and I do not mind that. I stray a lot myself. I enjoy it. In fact, it kind of spices up the hearing. Otherwise, we would just be listening and asking routine questions.

But I want to be very careful that we do what is right, and we accelerate. The Deputy Assistant Secretary is still here, and I hope he will not let this thing drag too long. And that the message gets back to the Department of Transportation. If he left, half the audience would have gone. But the Department of Transportation is still here because he is still here. Maybe they will all get the message.

But I just am concerned from the statements I have heard here this morning that while DOT is considering the matter, the control of the airline could continue to go, its management thrown out, and the sale of its assets completed before decision was ever made.

Now, have the courts put any—you say they put the brakes on.

Mr. **Meyer**. They have put the brakes on temporarily.

Senator **Ford**. For how long, do you know?

Mr. **Meyer**. I do not know. There is a hearing Friday morning.

Senator **Ford**. So you have a hearing Friday morning, and the brakes could be taken off.

Mr. **Meyer**. Maybe, maybe not. I do not know. It depends upon what happens.

Senator **Ford**. And the 28th is the hearing by the Department of Transportation?

Mr. **Meyer**. It is not the hearing. It is just the filing.

Senator **Ford**. So, it is not a point where they can make any kind of an accelerated decision?

Mr. **Meyer**. No, sir.

Senator **Ford**. I do not know whether we ought to get into this kind of business or not, Madam Chairman.

Mr. MEYER. They can freeze. As I think I said, it is urgently needed.

Senator FORD. The Department can freeze what?

Mr. MEYER. The control of the company, the passing of control of the company or any further action.

Senator FORD. They would not prevent him from buying stock?

Mr. MEYER. That would prevent him from taking control, having tender, using a consent procedure and the like in order to take control and remove the board of directors.

Senator KASSEBAUM. That brings up an interesting question, because it seems to me that is an extraordinary step for the Government to take at that point. I would be curious just what you would envision DOT could do, even if they wanted to. They could not block the acquisition of stock, could they? Have they ever?

Mr. MEYER. My understanding is that they could block the change of control and freeze the situation as it sits now so that he could not exercise his stock to take control of the company. It is my understanding that could happen.

Senator KASSEBAUM. Under the fitness guideline and safety or under what authority?

Mr. MEYER. Under the fitness and safety. This is an extraordinary situation. This is the first time that this has happened to certainly an airline in a heavily regulated company, a company that has international route certificates.

Mr. ASH. Senator, there is——

Senator KASSEBAUM. I thought we were deregulated now. Everybody keeps talking about regulation.

Mr. MEYER. I am not trying to reregulate the industry. I am trying to provide the time for a hearing which I think is very necessary. And I would think that Mr. Icahn, if he is true to what he says in his letter, would stand aside and stand up to that hearing.

Senator KASSEBAUM. Well, I have no sympathy for the Mr. Icahns of the world. I think they have disrupted communities and companies. But what we need to do, I think, first and foremost is remove the tax incentives that have encouraged this type of behavior, and that is what it seems to me is the ultimate answer to this particular type of action.

Mr. ASH. Senator, if I might, there are certain—there is a belief that you possibly cannot or that the DOT possibly cannot order stock into a voting trust pending an outcome of a decision, or at least that that would be unique. But the fact is if anyone in this room decides tomorrow to start an airline, they may not go out and operate that airline until such time as they go in and demonstrate fitness, credible management, an operating plan, and a tendency toward compliance. And if that is a requirement in order to be licensed for all of the good reasons that are there, which include fitness, safety and in our case particularly international aviation, then one should not be able to go in the back door by just buying direct control and say ha, see, I got a certificate. And that is the basis of our argument that a fitness finding should be made, and our license ought to be conditioned and in effect locked so that we cannot operate or that he cannot gain further control until that finding is made.

Senator **Kassebaum**. Senator Ford, I interrupted really your questioning. Did you have anything further?

Senator **Ford**. No. I was enjoying yours.

Senator **Kassebaum**. I would like to just ask one question on the purpose of this hearing, and that is the extent of TWA's international authority. To what extent is your international certification temporary?

Mr. **Meyer**. Let me state it the other way around. With the exception, I believe, of Paris and Rome, our other certificates are temporary.

Senator **Kassebaum**. Thank you very much, Mr. Meyer. We appreciate your testimony.

Mr. **Meyer**. Thank you, Senator.

[The following information was subsequently received for the record:]

Questions of Senator Hollings and the Answers

Question. Mr. Meyer, how many routes does TWA now fly with permanent certification? How many with temporary/experimental certificates?

Answer. For the record, I should state at the outset that TWA does not possess any "permanent" international route authority, and I think that this is an important point that has been largely misunderstood in the context of the proposed legislation. TWA holds "indefinite" certificate authority for and is serving the following international points: Paris, Rome, Athens, Geneva, Zurich, Frankfurt, Munich, Copenhagen, Amsterdam, Cario, Vienna, Barcelona, Brussels, Tel Aviv, Kuwait and Bombay. We also hold "temporary" authority, which we have had to get renewed periodically at great time and expense to not only TWA but to the Federal Government for certain U.S. gateways and such important points in Europe as London, Lisbon, Madrid and Milan, all of which we serve today.

The DOT already has ample power to act quickly, consistent with due process requirements, to suspend a carrier's indefinite authority in the event of service deficiencies. All we are really seeking here is legislation which will convert our temporary authority, and the temporary authority of other similarly situated carriers, to indefinite—not "permanent"—authority, thus obviating the mechanical drill of having to go through renewal hearings on a preset, periodic basis. The DOT will still have the authority to remove carriers from routes when warranted.

Question. As you heard earlier, during Mr. Shane's testimony, DOT is planning a rulemaking on the issue of international route certificate duration. Would this be a satisfactory means of addressing this issue for TWA?

Answer. No. The proposed legislation is in the nature of a congressional policy directive to the DOT to cease expending taxpayers dollars in seemingly endless and time consuming renewal cases. If the DOT should engage in a rulemaking proceeding and issue a rule which tracks the proposed legislation, fine. But who is to say that the DOT would do so, absent a nudge from Congress? There is nothing to prevent the DOT from issuing a rule to the effect that the renewal process should continue indefinitely, and then we'd be right back on the treadmill. We are simply requesting that you direct the DOT to convert temporary authority to indefinite authority. We would expect in such event that the DOT would still issue a rule setting forth the criteria and procedures involved in cases under section 401 of the Federal Aviation Act looking toward the termination of indefinite certificates.

Question. Can you tell the Committe how much money TWA has spent in the past in defending its existing certificates during the CAB renewal proceedings? How many times has your airline been subject to this type of challenge? If this information is not available today, please provide it for the record.

Answer. A not atypical example was the Transatlantic Route Renewal Proceeding that took place in the mid-1970's. TWA's legal fees to our outside law firm in that case were $514,723. In addition, TWA's Regulatory, Marketing, Finance, and Legal Departments expended many, many hours over the two and one-half year span of that route case. Legal fees and other costs have increased substantially since then and future renewal expenditures could exceed that figure.

In 1945 the Civil Aeronautics Board awarded TWA its basic transatlantic route certificate, which was amended in 1950. TWA's route authority was renewed in protracted proceedings in 1962, 1966, 1973 and 1977. We are presently facing yet another renewal proceeding in connection with our certificate expiration in March of 1986. TWA's transatlantic route authority was challenged in all of these renewal proceedings. However, TWA never lost a route as a result of such challenges. These proceedings were most time consuming. For instance, the CAB instituted the 1966 route renewal proceeding in May 1962. The hearing went on for several months and the final decision wass not reached until 1967. We estimate that our legal fees in that proceeding were almost as large as those we were forced to expend in the renewal case that took place in the mid-1970's.

Question. Has TWA ever challenged another U.S. air carrier's route certification at the time of its renewal?

Answer. The only instance I can recall was in 1964 when TWA challenged, unsuccessfully, Pan Am's authority for the Iberian Peninsula.

Question. Does TWA support the sale of international airline certificates between U.S. carriers, such as being proposed between Pan Am and United Airlines?

Answer. TWA is a party in the PA/UA case involving the sale of Pan Am's authority to United, and we have not yet taken a position with respect to that transfer. Generally speaking, without commenting on the specific merits of that case, we are of the view that, in the absence of major anti-competitive ramifications, permitting transfers of route authority is consistent with deregulation, and both are consistent with indefinite certificate authority. Of course, such transfers are subject to prior approval by the DOT, and this is as it should be. On the other hand, if a carrier has been providing continuous service in a market and is an effective competitor, there is no reason whatsoever for the DOT to run that carrier through a series of renewal cases. And this is why we are advocating that our transatlantic temporary route authority be made indefinite.

QUESTIONS OF SENATOR INOUYE AND THE ANSWERS

Question. How many times has it been necessary for TWA to go through renewal proceedings on its transatlantic and other routes?

Answer In 1945 the Civil Aeronautics Board awarded us our basic transatlantic route certificate. It was amended in 1950 and renewed in 1952, 1966 and again in 1977. We face yet another renewal proceeding in connection with our certificate expiration in March 1986.

Question. Has TWA's route authority been challenged on many of these occasions? Has TWA ever lost any international route authority in its renewal cases?

Answer. There have been such challenges, but we have never lost route rights as a result. For example, in the most recent such case, one CAB bureau advocated an area concept which would have stripped TWA of its right to serve Germany and all countries east of Italy. Similar harsh adjustments were proposed for Pan American's transatlantic route network. In addition, another applicant (National) wanted the CAB to remove TWA from the London and Frankfurt markets and to cancel our Africa authority. The CAB rejected these proposals.

Question. How costly are these renewal cases and what amount of time and effort are required by the airline?

Answer. Such cases are very burdensome to the participants. In the last transatlantic renewal case—the one which cost us a half million dollars in legal fees—TWA also ran up large bills for printing, postage and clerical assistance, and devoted thousands of management man-hours over the two and one-half years span of the case to the preparation of evidence, testimony, briefs and participation in the hearing before the Administrative Law Judge. These were man-hours which could have been spent much more productively running the airline. To the bese of our knowledge, no carrier has ever lost a route as a result of a challenge under a route renewal case. In the end, then, the renewal process is an expensive, functionless drill.

Question. What effect does the renewal process have on an airlines' flexibility in providing international service and making the long-term decisions necessary to establish itself in a route?

Answer. Fleet planning is the major long term planning issue that is affected by the renewal process, especially with regard to temporary, experimental certificate authority under Section 401(d)(8) of the Federal Aviation Act. The long range aircrafts that are needed in order to operate on an international route are very expensive. Similarly, such authority is a deterrent to making the expensive investment necessary to provide expansive service.

Question. Do you feel that the bumping procedure laid out in S. 586, combined with existing DOT authority to remove carriers if they are not providing adequate service on a route, is a sufficient incentive to incumbent airlines to be competitive and provide the best service possible?

Answer. Yes. The bumping procedure and the existing DOT authority to remove carriers provide adequate regulatory incentive to incumbents to be competitive and to provide the best service possible. The renewal process adds no incentive.

Under the bumping procedure and existing DOT authority, a carrier's performance on routes in foreign air transporation would be scrutenized when there is a need for it, not when an arbitrary renewal date rolls up on the calendar. The DOT has the ability, upon petition, complaint, or its own initiative, to suspend, modify or revoke, after a hearing if required, certificates for non-compliance. Based on such findings a carrier's designation to serve a foreign point may be removed, thus rendering the certificate or license useless. In addition, the regulatory agency must approve fares and rates in foreign air transportation and it can suspend a fare or rate pending a determination of its lawfulness.

With the bumping procedure, this means that if a carrier is failing to meet it obligations, the Board has ample power to deal with a service problem when it arises. This is far more practical and less costly than going through a burdensome renewal drill at the inflexible command of the calendar regardless of the service actually being provided. The Board can institute certificate suspension proceedings at any time during the effectiveness of a carrier's authority. Requiring it to do so based on some arbitrary date is a redundant regulatory intrusion that adds nothing to this process except unnecessary waste and expense.

Question. Do you feel that U.S. carriers are put at a disadvantage because they have to go through the renewal process periodically and foreign carriers do not?

Answer. Yes. The foreign flag competitors of U.S. carriers never face a route renewal problem, because their authority tends to be permanent. Having to participate in periodic route renewal proceedings when our foreign competitors do not puts U.S. carriers at a competitive disadvantage: during the several or half a dozen years that a renewal proceeding is in progress, U.S. carriers' resourses, including their management staffs, are tied up with defending their route authority, while the foreign carriers, including their marketing and planning staffs, are concentrating single-mindedly on competing in the market.

Moreover, there are major inconsistencies in the existing international route authorities held by various U.S. carriers. Between the U.S. and Europe, for example, TWA has indefinite route authority to Paris and Rome and has temporary authority to London and Lisbon, while the authority of Pan Am to London and Lisbon is permanent but to Paris and Rome is temporary. TWA, a major U.S.—London carrier, is forced to defend its U.S.—London authority at periodic intervals, while its competitor, both U.S. and foreign, are free to devote their resources to competing on the route. All U.S. carriers should be put on a par with indefinite certificate authority.

Senator **Kassebaum**. If there are no objections, we would like to call the next witnesses. Mr. Hitchcock, would you mind joining in a panel discussion with the other witnesses, which would be yourself, Mr. Cohn representing People Express, and Jeff Manley representing TransAmerica Airlines.

Senator **Ford**. Madam Chairman, I would like to make the observation that DOT left.

Senator **Kassebaum**. DOT left and so did almost the rest of the room.

It is a pleasure to welcome the three of you, and we appreciate your joining forces at this point.

Mr. Hitchcock, we will start with you.

STATEMENT OF CON HITCHCOCK, AVIATION CONSUMER ACTION PROJECT

Mr. **Hitchcock**. Thank you, Madam Chairman.

I find myself in a somewhat awkward position for two reasons. First of all, I am not sure I could say anything as dramatic or timely as the previous witness; and second, I find myself in the position of testifying in opposition to a bill with such a distinguished list of sponsors.

Nonetheless, we would respectfully urge the committee and the subcommittee to reconsider the need for this legislation. I think it is important to put this issue in context from the standpoint of the traveling public. When you are dealing with limited entry markets, the Government is giving a carrier a legalized shared monopoly. Viewed in that context, temporary certificates are an important means of consumer protection, because if travelers are going to be stuck with a given airline on a route for 5 years or 10 years, maybe more, there has to be some kind of safety valve. Otherwise the incumbent may grow complacent and let its service deteriorate.

When viewed in this light, legislation to transform these limited duration certificates into permanent certificates is a step in the wrong direction. If any bill is going to be passed, we would agree with the suggestion that was made last year by People Express and that Mr. Cohn may discuss, that permanent certificates should be made temporary, not the other way around.

From our experience we have not seen any evidence that limited duration certificates impose any real burden on airlines or limit their ability to develop markets and to compete with foreign competitors.

I recall from taking part in various bilateral negotiations there were times when the United States stood to gain a new route from the negotiations, and the message from our carriers to the negotiators was not, "This is going to be a difficult route to serve because we can only get a 5-year license" or that "This route really is not worth it."

The message that our airlines always gave to the negotiators was, no matter how economically chancy the route, "Get us this route; we will find a way to serve it." That really is how valuable these routes are and why it is important that some care be taken to make sure that the public is well served on them.

As a practical matter, we do not think that carriers would have much to worry about if temporary certificates were continued as a policy, provided they continue to give good service. The CAB certainly did not yank certificates willy nilly in the past, and we do not think that DOT would act capriciously in deciding to substitute one carrier for another on a given route.

Now, of course, this brings me to the bumping provision in your legislation. The language in the bill is an improvement over the proposal considered last year by your colleagues on the House side, but we think it still tilts too far in favor of the incumbent airline. The types of judgments that you are asking the Secretary to make can be made and made well in the temporary certificate process, particularly if DOT goes through the rulemaking procedures that Mr. Shane described earlier. I am speaking particularly of the standard that a challenger has to meet, of a "substantially improved" combination of service and fares or rates in the market, which may be difficult to achieve as a practical matter. For example, some countries may restrict the number of flights, so a carrier cannot really compete with more frequencies, or it may severely limit price competition, so a new entrant cannot come along and say, we are going to offer these discount fares or a standard low fare service, or a country may restrict new entrants using a secondary airport, thereby limiting its ability to compete with an established airline at the major airport where might have some kind of hub and spoke or fifth freedom rights.

The requirement of on-the-record hearings means there has to be full-blown trial-type proceeding, and that is rather ironic considering that the thrust of the comments has been on how we have to cut down on legal fees and cut down on legal proceedings.

And finally, your subpararaph (c) gives the Secretary too much latitude to squelch new service proposals. When you have a system of temporary certificates, the certificates are reviewed in a regular orderly basis, and it is at one point every 5 years or so that applications come in to be considered if anyone wants to challenge an incumbent. If you have permanent certificates there is definitely a problem that people can come along at any point, and how is the Secretary going to deal with them.

Our concern is that the language in your bill is so broad that the Secretary has virtually unfettered power to deny applications summarily, regardless of their merit.

Now in the ordinary course of things an applicant to an agency who is turned down often has a right of judicial review, if the applicant can show that the agency abused its discretion or failed to follow the statute. But the language of the bill is so open-ended that I doubt there would be any real relief from a court, and you might have a situation where the bill could be administered in a protectionist closed door policy.

To close, I would like to return to the key question, which is, "Is legislation really necessary?" and I think the answer must be "no." The discussions last year on the House side, which Mr. Meyer alluded to, expressed the concern of some carriers that licensing proceedings cost too much, and the figures bandied around suggest that the cost to a carrier is about $40,000 or $50,000.

Let me put that item in perspective. According to a recent article in Aviation Daily, Pan American announced it was going to be spending a million dollars to refurbish the cabin of each 747, its business class. Now, if they can spend a million dollars to refurbish the cabins of business class, how can they say it's hideously expensive to spend $40,000 for the right to keep flying that airplane to a foreign destination?

Don't get me wrong. As a consumer group we favor cutting inflated legal fees wherever possible, but in this case the purpose of these types of proceedings is very important. It is to prevent the public from being saddled with poor service and few, if any, alternatives for a very long period of time. And considering the potential profits at stake for an airline, the money that the carrier has to spend to defend its license seems truly modest by comparison and more than justified.

If the present policy continues, we doubt that those airlines which do a good job of serving the public will have little to fear. The arguments I have heard here are like the arguments made about deregulation. Those carriers that do a good job will probably do well in a deregulated environment. Those that do well in international service are probably not going to have too many challengers nipping at their heels by making serious efforts or credible efforts to bump them from a route. The only carriers who may have to worry are those carriers who are not doing all that they can, and as far as we see it, that means the system is working, if contested hearings produce enough evidence for DOT to make a correct decision on which airline best serves the *public* convenience and necessity.

I appreciate the opportunity to be here, and I would be happy to answer your questions.

[The statement follows:]

STATEMENT OF CORNISH F. HITCHCOCK, LEGAL DIRECTOR, AVIATION CONSUMER ACTION PROJECT

Madam Chairman, Members of the subcommittee: On behalf of the Aviation Consumer Action Project (ACAP), I appreciate the invitation to testify today on S. 586, which would give permanent certificates to U.S. air carriers holding temporary licenses to serve international markets.

Founded in 1971, ACAP is the only non-profit consumer organization working full-time on aviation matters. We have taken part in agency proceedings on international aviation issues and have testified before Congress on this topic. In additon, we served for several years as a public member of U.S. delegations negotiating air transport agreements with foreign countries.

ACAP has long supported a pro-competitive policy in international aviation. We believe that encouraging price competition and service options is the best way to serve the needs of the traveling public. We recognize that such a policy is not always easy to achieve, given the philosophical differences which divide the United States and many of its aviation partners. Nonetheless, we believe that the breakthrough bilateral agreements of the late 1970s and IATCA's affirmation of competition as the principal goal of U.S. policy in this area have worked to the benefit of travelers and airlines alike. Consumers now have more choice about where they can fly, on what airline, and at what price. This represents a major step forward, when compared to the more limited range of options which consumers faced for many years.

Unfortunately, the picture is not uniformly rosy. Many countries sharply limit the number of carriers that can serve a given route, and a number of markets are nothing more than a shared monopoly: one U.S. carrier and one foreign carrier. Entry restrictions affect travel along routes to such major destinations as Canada, Mexico, the United Kingdom and Japan. As a result, passengers have limited choices in these and other markets, and thus only a limited ability to take their business elsewhere if service is poor.

To help remedy this situation, the Civil Aeronautics Board began imposing five year limitations on certificates to serve limited-entry markets. This policy alerts carriers to the fact that the quality of their service will be periodically reviewed and that they can be replaced if their service is not up to par. These temporary certificates constitute an important means of consumer protection. If travellers are going to be stuck with a given airline on a route for five years and possibly longer, there has to be some kind of safety valve. Otherwise, the incumbent may grow complacent and let the quality of its service deteriorate, since there is no risk of new entry.

When viewed in this light, legislation to transform these temporary licenses into permanent certificates is a step in the wrong direction, and we see no justification for such a move. If any bill is going to be passed, we would agree with the suggestion made last year by People Express that all permanent certificates should be made temporary, rather than the other way around. Whenever the CAB and now DOT bestows a route award on a carrier, it is giving away a potentially valuable right. It is bad public policy for the government to give away valuable rights without at least some meaningful check or restraint that helps to assure that the public will be well served by this legalized monopoly.

Moreover, we have seen no evidence that certificates of limited duration impose any real burden on airlines or limit their ability to develop a market and compete with foreign flag carriers. I recall various bilateral negotiations where the United States stood to gain a new route to a particular country; not once did a U.S. airline tell our negotiators not to bargain for the route because it might be expensive to serve or because the designated U.S. airline could only obtain a five year certificate. Instead, the carriers' message to our negotiators was always, "Get us the route, and we'll worry about how to serve it." That is how valuable these route rights are, particularly in limited-access markets.

If the policy of temporary certificates were to continue, it is unlikely that these licenses would be yanked frequently, if at all, once the designated time period is up.

Certainly, the Board did not revoke certificates willy-nilly in the past, and we doubt that, in the absence of legislation, DOT would act capriciously in substituting one carrier for another on a given route.

That brings me to the "bumping" provision in S. 586. While this language is an improvement over a proposal considered last year by the House Aviation Subcommittee, we think that it tilts too far in favor of the incumbent airline and does not provide a meaningful check on the problems I have discussed. Moreover, the types of judgments and decisions which this bill asks the Secretary to make can be made and made well whenever a temporary certificate is up for review.

In particular, the standard which a challenger must meet—"a substantially improved combination of service and fares or rates in the market"—may be impossible to achieve, as a practical matter. For example, a country may restrict the number of flights which can be offered on a given route, thus eliminating any chance of competing with more frequent flights. Or a country may severely limit price competition (Japan is a notable example of this), with the result that an applicant cannot realistically promise that it is going to slash fares if it takes over the route. Or a country may restrict new entrants to using a secondary airport, making it impossible for that challenger to "substantially" improve the service of the incumbent which uses the primary hub airport.

Second, the requirement of an "on the record" hearing means that there must be a full-blown trial-type proceeding every time an application is considered on the merits. This provision is rather ironic, since the principal complaint from the carriers at last year's House hearing was that CAB licensing proceedings cost too much.

Finally, subparagraph (C) of this bill gives the Secretary too much latitude to squelch new service proposals without a full hearing. That provision deals with a problem that is inherent in any discussion of revoking a permanent license: if an applicant is free to file a challenge at any time, there ought to be a mechanism to weed out the insubstantial proposals from the more serious ones. Subparagraph (C) specifices those circumstances in which a Secretary can reject a proposal without a hearing. Our concern is that the lanugage here is so broad that it gives the Secretary a virtually unfettered power to deny applications summarily, regardless of their merit. Ordinarily, when an agency denies an application for a license, the disgruntled applicant can ask a court to review that decision, and the applicant has to show how the agency abused its discretion or acted beyond the scope of its statutory authority. The language of this bill is so open-ended, however, that I doubt a reviewing court would overturn the Secretary's decision and direct that a hearing be held. The result could be a very protectionist, closed-door policy toward competition from new entrants.

In closing, it is important to ask, "Is this bill really necessary?" I think the answer must be "no," and we would urge you to reconsider this legislation. As I mentioned a moment ago, the motive force last year seemed to be the concern of some carriers that licensing proceedings cost too much, and the figures bandied about suggested that the cost to carriers is about $40,000 to $50,000. In our view, cutting these fees is not a valid reason for Congress to give incumbents a permanent shared monopoly on certain routes, even if they can theoretically be "bumped" by a new entrant.

Don't get me wrong. As a consumer group, we favor reducing inflated legal fees whenever possible. But it is important to place this question in context. The purpose of these renewal proceedings is to prevent the public from being saddled with poor service and few if any alternatives for a number of years. Considering the potential profits at stake, the money which an airline must spend to defend its license is truly modest by comparison and more than justified.

If the policy of temporary licenses in limited-entry markets were to continue, we suspect that those airlines which do a good job of serving the public will have little to fear, either in terms of the cost or the time expended. This conclusion is re-inforced when one considers the flexibility which DOT has to use "show cause" and other simplified procedures. The only carriers who may have to worry are those airlines who are not doing all they can to serve their customers. If these carriers have to pay more to defend their performance, that simply means that the system is working. It also means that DOT will have enough evidence to make an informed decision on which of the airlines seeking to serve a route will truly serve the "public convenience and necessity."

Thank you again for the opportunity to be with you this morning. I will be happy to respond to your question.

Senator KASSEBAUM. Thank you, Mr. Hitchcock. If it's all right with you, Senator Inouye, I think we will hear from everybody and then ask questions.

Mr. COHN.

STATEMENT OF ROBERT E. COHN, GENERAL COUNSEL, PEOPLE EXPRESS AIRLINES

Mr. COHN. Thank you, Madame Chairman, Senator Inouye. I am Bob Cohn. I am General Counsel of People Express Airlines. I very much appreciate the opportunity to testify today on what we see to be a very important issue in international aviation policy. People express strongly opposes converting temporary certificate authority in a limited entry into international markets into ones of indefinite duration.

We believe the proposal is anticompetitive, anticonsumer, and should be rejected as special interest legislation that will benefit a very few companies to the detriment of the overall public interest.

The underlying philosophy of airline deregulation which was endorsed by Congress in the Airline Deregulation Act of 1978 and the International Air Transportation Competition Act of 1979 is that airlines must have the freedom to enter any routes they wish, since free entry and free pricing provides a policing mechanism to ensure that carriers will behave in a fashion consistent with the public interest.

In short, it is freedom of entry that has replaced government regulation to protect consumer interest. Indeed, it was airline deregulation that provided the opportunity for People Express to come on the scene. We owe our very existence to airline deregulation and the pricing and entry freedoms that were provided and mandated by that statute.

In international markets, however, entry is often restricted by foreign governments which insist on limiting the number of carriers each country can designate over particular routes. Temporary certificates, in our view, are an integral component of deregulation and an important tool in maintaining competition in international aviation markets.

In entry-restricted international markets, the only realistic means by which the agency entrusted with regulating international air transportation, that is, the DOT, the only way they can replicate the competitive stimuli in any real fashion is by use of fixed-term temporary certificates.

This type of competitive mechanism does not constitute burdensome or intrusive government regulation. It is regulation designed to enhance competition in situations where the marketplace is artifically constrained. Enhancing competition is precisely the objective that Congress has mandated, and I will note at this point that People Express's only international certificate between Newark and London is a temporary certificate. We would benefit to the extent that the temporary certificate we have between Newark and London would be made indefinite.

But yet, we also see that that is not (a) in our long-term best interest because we want to have an opportunity to compete for some of these very valuable and limited and lucrative international routes that some of the carriers are holding. And we think that we will be prevented from doing so if the temporary certificates are made indefinite.

We think the temporary certificates provide a number of important public interest benefits, and I would like to tick some of those off. First of all, the expectation and certainty of a renewal review and a threat of potential competing applications will force the incumbent to behave in a fashion most conducive to the interest of the traveling public. Renewals will discourage incumbents in limited entry markets from exploiting consumers and engaging in monopoly-type practices and abuses.

In short, the temporary duration provides a self-disciplining mechanism to encourage the incumbent to perform well in order to protect its stake in the market.

Second, short-term certificates provide an important opportunity for new carriers to gain access to important international markets by allowing carriers such as People Express and others to demonstrate that they can better meet the DOT's competitive market structure objectives and provide better, more innovative services that will offer the traveling public greater benefits than the incumbents.

Many of the existing temporary certificates were awarded before airline deregulation was passed, before many of the new entrant carriers came on the scene. People Express and others want to have the opportunity to vie for some of these lucrative limited entry routes under today's changed aviation policies and economic circumstances.

Third, temporary certificates will keep applicants honest in the carrier selection process before DOT in these limited entry routes. Their proposals will have to be realistic and achievable since renewal proceedings will be just around the corner and they are going to have to defend their market behavior.

People Express has had a tremendously successful operation between Newark and London for which the public demand has been enormous. As People Express's wide body fleet expands, we want to have that ability to take on other international opportunities and to expand the frontier of low fare international services.

Permanent certificates will effectively foreclose these opportunities for new entrants in the most valuable limited entry routes. The administrative and legal hurdles of convincing a regulatory agency and overcoming the inertia of an agency not to do anything under current law and even under S. 586 will basically foreclose the opportunity for new carriers to get into the marketplace.

DOT cannot revoke authority today under current law unless there is an intentional violation committed by the air carrier—that is under Section 401(g)—and that air carrier was given an opportunity to correct the violation. And clearly, if an incumbent carrier asked for an oral evidentiary hearing, should there be a request to have that authority suspended or revoked, you can bet that they will make use of every process they can to prevent a new entrant from using existing law to effect the replacement.

While S. 586 has a bumping mechanism built into it, the decisional standard in my view is virtually impossible to establish. The practical effect of converting temporary certificates into permanent certificates even under legislation similar to S. 586 would be to erect a virtually impenetrable administrative barrier, shielding incumbents from the rigors of the competitive process.

If legislation on this subject is needed at all, People Express would urge that all permanent certificates be converted into temporary certificates. This would certainly maximize competitive pressures throughout the international arena. It will eliminate that inconsistency problem, Senator, that you raised earlier concerning some carriers holding permanent and some carriers holding temporary certificates.

We believe that certificates awarded in prior regulatory eras under totally different statutory policies and objectives should be reviewed under today's changed public interest standards.

Now, the proponents of this legislation have raised in our view a number of specious arguments. We have heard some this morning. They argue that the renewal proceedings represent a waste of time, a waste of money, and administrative resources. And I think that their claim is erroneous.

First of all, they cite to the one case which is not illustrative at all of what happens on today's streamlined administrative processes after deregulation. The Transatlantic Route Renewal case was prederegulation. It took years to litigate. It was litigated under a public convenience and necessity standard which predated the current competition standard. It was a protectionist standard, and it had every single transatlantic route, scheduled and charter. It also included the entire panoply of charter policy regulations—the case in which, incidentally, I was Bureau counsel at the time when I worked at the CAB during that proceeding.

It just simply will not be repeated again in today's procedural process. It just won't happen. And in fact, DOT has the ability to streamline the process under law that was provided to it under the Airline Deregulation Act. The DOT can initially propose to renew all of the certificates by show cause order, and in many of these cases they will be uncontested and the renewals will continue without much process at all.

In the contested markets, the Agency is not required to hold a full oral evidentiary hearing. It could use simplified nonoral hearing procedures. I must say, ironically, it will probably be the incumbents who will insist that the full panoply of adminstrative procedures be used, hoping that long and expensive procedures will ward off potential competitors.

And I think that the real focus of cost should not be on the cost to the incumbent carriers who hold these limited rights, but on the cost to the traveling public and to consumers who will be, in our view, abused by the process of creating essentially permanent certification.

The second argument that you hear is that the temporary certificates make planning and acquisition and financing of these routes very difficult. That claim is also without merit. Essentially since 1978, all international certificates in limited entry markets have been temporary and this hasn't deterred any airlines who have been applicants for those routes from obtaining the necessary financial and operational resources with which to commence and operate that service.

It certainly didn't prevent People Express, which is operating under a 5-year temporary certificate between Newark and London, from starting that service and doing, as far as I'm concerned, a bang-up job on that route.

Third, you will hear the proponents will argue that it is unfair for some U.S. carriers to hold permanent rights while others don't. I really think that argument is a red herring, and if you want to cure it, you can cure it by making all of these certificates temporary, but in fact it—we compete against four major airlines—British Airways, British Caledonia, TWA, and Pan American, all of whom hold permanent rights in the New York/Newark market and that has not prevented People Express from gaining very strong competitive foothold and from keeping that foothold, and we are not concerned that in a few years we are going to have to be subjecting ourselves to a renewal proceeding, because we are doing a good job. And we are willing to test in the rigors of any process our capability of continuing to do that job.

Finally, the proponents argue that it is unfair for U.S. carriers to compete against foreign carriers, many of whom hold permanent rights, some of whom are owned by foreign governments. The fact is that most foreign governments have different philosophies with respect to aviation policy than the U.S. Government.

Few, if any, foreign governments are as deeply committed to maximum reliance on competition as a major regulatory force and the fact that a foreign government issues permanent authority to its carriers in my view does not justify withdrawing from what we believe to be sound public policy.

I would like to turn briefly to S. 586 to indicate some of the deficiencies I see. I must say the bill is an improvement over what we had seen last year in hearings before the House, because it changes the standard from one "required by the public interest" to one "consistent with the public interest," and it has a bumping provision in it.

However, in my view, the bumping provision does not—it still creates a barrier. It is not a reasonable bumping provision and the reason is that it requires the applicant to demonstrate that it can and will provide substantially improved service and fares, a combination of both.

In many limited entry markets, the fares and capacity are really strictly regulated and in fact it is going to be very difficult for a new entrant carrier or an applicant to actually be able, at least initially, to operate perhaps higher service, at higher levels of services, or maybe charge lower fares.

And the important lead is for that reason, is that in DOT carrier selection cases, that is not the principal carrier selection element. Rather, they look to more fundamental criteria relating to market structure, to the competitive market structure when they select the carrier because that is the market structure that basically will create the incentives for that carrier providing the higher level of service.

They use competitive market structure. They look at the ability of the carrier at a particular gateway to garner traffic flows, to have a flow of traffic that will capture the most online connecting services to support that new gateway service. And basically they look to maximizing intergateway competition.

These are the criteria that DOT uses, and frankly while we oppose this legislation, we think it is not necessary if you are going to adopt a structure that has permanent certification or indefinite certificates. We think that the bumping standard ought to be a standard that is keyed to the carrier selection criteria used by DOT in its current international route cases, rather than a much more limited, in my view, unreachable standard that is now set forth in S. 586.

In conclusion, People Express believes that the proposal is really not the subject or not the proper subject of legislation by Congress. Congress entrusted DOT to oversee international aviation route proceedings, and while DOT's predecessor, the Civil Aeronautics Board, has correctly in our view determined that in limited entry markets temporary certificates is the method most consistent with the interest of the traveling public, DOT has not yet addressed the issue.

And we heard this morning that they expect to shortly issue a rulemaking on that. We would urge the committee not to intervene in this area at this point. We think the whole idea ought to be rejected as basically anticonsumer and anticompetitive.

That concludes my presentation, and I will wait for questions a little later on.

[The attachment referred to follows:]

10(A) On and after the date of enactment of this paragraph, an expiration date in any certificate or portion thereof authorizing foreign air transportation which was issued under this Section shall, subject to the provisions of subparagraphs (B)-(F) of this paragraph (10), be of no effect and such certificate or portion thereof sti[illegible] be deemed to be of indefinite duration.

(B) Subparagraph (A) will not be applicable to temporary certificates authorizing nonstop service with respect to a particular restricted foreign air transportation market or markets in which the holder does not provide such service. A restricted foreign air transportation market is a market as to which restrictions arising from the provisions of a bilateral air transport agreement or other agreement or understanding, or which are otherwise imposed by a foreign country, preclude, prevent, impair, or make it impracticable for the Secretary to authorize and/or designate an additional air carrier or carriers to serve the particular foreign market or markets.

(C) In the case of any certificate or portion thereof to which subsection (A) of this Section applies, the Secretary of Transportation may, upon petition or upon the Secretary's own motion, review the authority to the holder of the certificate to provide foreign air transportation and take the following action:

(1) The Secretary may, after notice and hearing, include an expiration date in any such certificate or portion thereof if the Secretary finds such action to be consistent with the public convenience and necessity and the public interest; and/or

(2) The Secretary may suspend such authority and grant authority to provide such foreign air transportation to another qualified air carrier, if the Secretary finds, after notice and hearing, that (1) the holder has not used the authority or (2) on the basis of the same carrier selection criteria used by the Secretary in *de novo* route cases, another air carrier should be selected and issued authority to serve the particular foreign air transportation market or markets in lieu of the holder; *provided* that the Secretary also finds that:

(i) restrictions arising from the provisions of a bilateral air transport agreement or other agreement or understanding, or which are otherwise imposed by a foreign country, preclude, prevent, impair or make it impracticable for the Secretary to authorize and/or designate an additional carrier or carriers to serve the particular foreign market or markets; and

(ii) suspension of the authority of the holder and grant of such authority to another qualified air carrier will be consistent with the public convenience and necessity.

(D) The Secretary may dismiss any petition filed under Paragraph B of this subsection if the Secretary finds the air carrier applicant or applicants would be unlikely to prevail on the carrier selection merits in such a proceeding and that the public interest otherwise requires such dismissal.

(E) The authority of the Secretary under Paragraphs (B), (C) and (D) of this subsection shall be in addition to, and shall in no way limit, the Secretary's existing authority under Paragraph (8) or subsections (D) and (G) of this Section.

Senator **KASSEBAUM**. Thank you.

Mr. Manley.

STATEMENT OF JEFF MANLEY, REPRESENTING TRANSAMERICA AIRLINES, INC.

Mr. **MANLEY**. Thank you, Madame Chairman.

I am Jeff Manley, representing Transamerica Airlines here this morning. As most of you know, Transamerica began its life as a supplemental carrier, as it was then called in the days after World War II.

It is now a charter and scheduled carrier with diversified operations involving both passenger and cargo services in numerous domestic and international markets. We view with considerable concern the concept now being proposed by several carriers under which their temporary route authority in international markets where entry is limited by foreign policy constraints would be converted into some sort of permanent authority.

Any legislation enacted to accomplish this would, we think, represent the first step away from a policy of deregulation which is a policy that Transamerica supported even before the concept had a name.

The proposals, as Bob Cohn said, are really nothing more than special interest legislation. They would help a few carriers to convert outstanding temporary routes, but basically the public and other carriers would suffer.

The arguments raised for legislative conversion are based primarily, it sounded to me like, on the cost of the regulatory renewal process. That is a red herring. The cost comparisons, as Mr. Cohn told you, are derived from old cases that are not going to be repeated.

The standards in those old cases really allowed the incumbent carriers, as they then were, to use the administrative process to block new entry to their routes, so in addition to renewing what they had, they were paying their lawyers and economists to keep other people out of markets.

And if you could break down the costs that they gave you, you would find that the big bucks were really spent hiring lawyers to block new people from coming in to compete with them.

Now, that was easy to do under the old standards where the administrative agency had to find that the public convenience and necessity required new entry. That allowed their lawyers to come in and prove that if there were new entry in that market, it would not help anyone. It would simply divert revenue from them and they would suffer, so therefore the public convenience and necessity did not require new entry.

Those standards have all changed. They cannot hire lawyers and economists to make those proofs anymore because they are irrelevant. The renewal process is now narrowed down to the question of whether someone who was given a route has done a proper job of serving it, and that is a much easier case to make.

These issues of keeping other carriers from competing with them are not there, because you are only going to have a renewal proceeding where the bilateral agreement limits the entry per se to one or two or whatever carriers. That is not a question to be proven or not proven in the proceeding.

Now, the conversion of the routes as proposed in S. 586 would, as I think you heard from TWA, encourage the kind of trafficking in international route authority that TWA on the other hand seems to abhor. The example was given of the spectacle of Pan Am's sale of its routes to United for some $750 million. Most of those routes that Pan Am is selling are permanent routes which they got back in the 1930's and 1940's, shortly after the Civil Aviation Act was passed.

If other routes that were granted later are converted to permanent status, this activity is going to be repeated many times over. And as TWA told you, it is not going to be limited to situations where one carrier is selling routes to another. It actually, according to them, sets up the airlines as potential attractive targets for these corporate raiders.

I was a little surprised when I heard TWA's testimony this morning because it sounds like they were testifying against this law. They were telling you that they are having difficulty getting DOT to hold off this corporate raider or whatever he is. But one of the things that has made them an attractive target is the route authority which they have which the corporate raider perceives as a valuable asset.

We believe that those routes in limited entry markets are in a very real sense a public resource that was negotiated by the United States for the benefit of everybody, and not just for particular carriers who end up having them awarded. I think Mr. Meyer made the point very effectively that the creation of those routes as a permanent fixture really does set up these people as these targets for takeovers.

If anything, I think what TWA told you this morning would seem to support the proposition that Mr. Cohn made under which you should be looking at legislation that would convert these outstanding permanent routes, which come from the old days of anticompetitive regulation, into the same sort of temporary route that would give the Government the power to control who is going to be operating it by constantly reviewing it under a regular procedure.

If a person looking to take over an airline sees that review or renewal coming on the horizon, it may be a less attractive target than it is now. Basically, we agree with DOT that this is a matter that is better left to rulemaking. In any event, we are not proposing any kind of legislation. We are not prepared at this point to endorse whatever DOT comes up with, but we think the committee should wait and give DOT a chance to get out a proposal and accept comment on it before moving foward with this.

If you do believe legislation is necessary, you should either adopt the alternative proposition which People Express has offered or look very carefully, given this situation created by the TWA takeover, at adopting legislation that would convert the outstanding permanent routes into the same sort of temporary routes that have been awarded since the Deregulation Act was passed.

Thank you.

[The statement follows:]

STATEMENT OF TRANSAMERICA AIRLINES, INC.

INTRODUCTION AND SUMMARY

Madam Chairman, members of the Committee, thank you for the opportunity to appear here today.

As most of you know, Transamerica Airlines began life as a supplemental air carrier in the post-World War II days. It is now a charter and scheduled air carrier with diversified operations involving passenger and cargo services in numerous domestic and international markets. It is a wholly-owned subsidiary of the Transamerica Corporation of San Francisco, California.

Transamerica has supported deregulation since well before the concept was popular or even had a name. Transamerica fought for legislation authorizing more competitive services from the time of the battles over charters in the 1950's and 1960's right through to the deregulation of the domestic and international air transport industries in the late 1970's.

Transamerica views with considerable concern the concept now being proposed by several carriers under which their "temporary" route authority in international markets where competitive entry is limited by foreign policy constraints would be converted into some form of "permanent" authority. Any legislation enacted to accomplish this would represent the first step away from a policy of deregulation under which the maximum reliance is placed on competition to govern carrier behavior.

These proposals represent blatant special interest legislation under which a few incumbent carriers would gain a windfall advantage from conversion of awards which they knew would be temporary when they applied for them. Any such conversion would be grossly unfair to those carriers which may have foregone the opportunity to apply for certificates because they were unwilling to accept temporary authorizations. Indeed, some of the outstanding temporary certificates are holdovers from the days when carriers such as Transamerica and other potential new entrants were effectively barred from even submitting applications for scheduled routes.

The arguments raised for legislative conversion based on the alleged cost of the regulatory renewal process are red herrings of the most obvious kind. The cost comparisons are derived from renewal case processed under the pre-deregulation standards. These standards allowed incumbent carriers, such as those now proposing conversion, to preclude new competitive entry on their routes by throwing up roadblocks in the guise of endless legal procedures. They were not so much assuring renewal of their routes as assuring that they would not have to compete over most of them. It was this anticompetitive instinct that led them to spend so much to participate in the so-called renewal cases. Since 1978 the certification standards have changed. The renewal process is considerably streamlined and there is no longer any incentive to use it to block new entry. There need be no repeat of the expenses lavished on these proceedings in the future.

Conversion as proposed in S. 586 would also encourage trafficking in international route authority. The recent spectacle of Pam Am's sale to United of several transpacific routes (most of which are permanent routes issued in the pre-deregulation era) will inevitably be repeated many times over if S. 586 is enacted. These routes are valuable economic resources and their value is based on their scarcity which is, in turn, a product of bilateral government-to-government negotiations. In a very real sense these routes are a public resource negotiated for the benefit of the nation as a whole, not individual airlines, and they should not be converted into private property rights for sale to the highest bidder. By maintaining the routes in temporary certificates, their status as a public trust rather than a private property right can be protected.

There is a sound public interest justification for making awards in limited-entry markets on a temporary basis and it would be contrary to fair play and normal standards of procedural due process to change the rules legislatively after these awards have been made. Transamerica, therefore, opposes the enactment of any legislation such as S. 586 that would convert outstanding temporary certificates to permanent status.

BACKGROUND

The concept of temporary route authorizations is an integral part of deregulation. In the period after deregulation the CAB articulated a clear rationale for the award of temporary authority in international markets. Such awards were made only in markets where competitive entry was limited by foreign policy constraints which restrict the number of carriers the U.S. may designate to provide service. Much of the temporary authority was issued under the provisions of Section 401(d)(8) which provides for an experimental period of certification during which the Board or its successor, DOT, may review the performance of the carrier selected to serve a limited entry route and determine whether it is maximizing competitive benefits. DOT has carried this policy forward in its post-sunset limited-entry route awards.

The requirement that a temporary route award must be reviewed in a renewal proceeding is in no way inconsistent with deregulation. Temporary certificates are properly used only where multiple entry is impossible and competitive market forces cannot determine pricing or capacity decisions. The award of authority in these limited-entry markets confers a *de facto* monopoly on a selected carrier comparable to a license to a public utility in a "natural monopoly" situation. The use of temporary authority in turn assures that competitive market forces may come into play at least to the extent of assuring that the certificate holder will realize that his performance will be reviewed when renewal comes around and that, if he is not performing up to competitive standards, a new entrant may seek to replace him. This provides an incentive to operate competitive levels of service at competitive prices.

Without temporary route awards a far higher degree of government intervention would be required to assure that monopoly positions are not being improperly exploited. This could require a more thorough review of pricing and capacity decisions than is presently undertaken by the DOT, which has continued the CAB's practice of relying primarily on the renewal factor to assure proper performance by temporary certificate holders.

There are several important international markets where entry remains limited by foreign policy constraints. These include three of the largest international destinations—Canada, Mexico and the United Kingdom. There are also other countries where varying degrees of constraints have led the regulatory agencies to maintain a policy of limiting entry such as Japan, Brazil, Italy, Spain, Venezuela, Argentina, and the People's Republic of China.

On the other hand, there are now several major foreign destinations where multiple entry is accepted as the norm and no resort to temporary certification is required. These include West Germany, France, the Benelux countries, Israel, Korea, Taiwan, and several others. Transamerica holds certificate authority in many of these multiple entry markets and since 1979 has exercised it by providing scheduled service to Ireland, France, West Germany, Israel, and the Netherlands. These services have been in addition to Transamerica's continued charter operations in these and other areas.

TRANSAMERICA'S POSITION

The legislative conversion of outstanding temporary certificates would in effect represent a breach of public trust between the Government and the travelling public under which the Government has acted to assure that no unfair advantage will be taken of a monopoly position. Without the threat of non-renewal, certificate holders in limited-entry markets may be tempted to return to the days of price setting by air carrier cartels and even resort to collusive capacity limitations. At least the Government will have to remain prepared to intervene to assure that such actions are not taking place. Whereas, there is little likelihood that carriers would engage in such practices with knowledge that their operations will be subject to scrutiny in renewal proceedings.

The public may also get short-changed in another way if temporary certificates are converted. Many of the holders of temporary certificates operate services in international markets out of several gateways. There will be occasions when these carriers will be tempted to downgrade service at one gateway by forcing traffic to move via one-stop or connecting service at another gateway served by that carrier. While that action may improve the efficiency of that particular carrier's services, it would also be unfair to the citizens of the downgraded gateways, particularly if another carrier is willing to operate superior service. The existence of temporary authority both minimizes the likelihood of such deterioration of service and facilitates the selection of a replacement where one is willing to operate higher grade service.

Contrary to the suggestions that have been made by the proponents of certificate conversion, renewal proceedings need not be unduly expensive or burdensome.

While it is true that in the 1960's and 1970's such proceedings often dragged on for several weeks and generated thousands of pages of testimony and exhibits and ran up substantial legal and consultant fees, the CAB streamlined its procedures substantially since then and DOT has followed suit.

Contested route proceedings now seldom last longer than 2 or 3 days. The issues are much narrower than in the past when most of the attention was paid to whether the public convenience and necessity *required* renewal or additional certification. The inclusion of this issue caused incumbent carriers to devote their resources to protecting themselves from entry by arguing that additional competition should not be added to the market because it would allegedly bring diversion of their revenues to new carriers. The arguments concentrated on renewing incumbents and keeping out additional carriers. It was the examination of this issue of how many (if any) additional carriers were required that ran up the bills. This issue has now been eliminated and the focus is instead merely on which carrier or carriers should be selected. The number to be selected is determined by the terms of an international agreement and is not open to argument.

Transamerica fully agrees that a temporary certificate holder which has been doing a demonstrably adequate job of providing capacity at prices commensurate with services in comparable competitive markets should have little to fear in a renewal proceeding. Indeed, expedited nonhearing procedures would probably be appropriate in most cases to renew such a carrier's temporary certificate. This could involve a Government review of the carrier's performance in advance of setting renewal proceedings. At that time a determination could be made that the performance has been adequate and an order could be issued directing interested parties to show cause why renewal should not be granted. A competing carrier would have a heavy burden to demonstrate why such a carrier should be replaced.

On the other hand where a temporary certificate-holder has provided less attractive levels of capacity and pricing than the market warrants or has otherwise neglected one or more markets in favor of others, there should be a procedure for allowing replacement of that carrier by one more willing to upgrade service at competitive prices. Renewal proceedings involving temporary certificates provide just such a procedure.

Conversion of temporary certificates to permanent status really only helps those carriers which have some serious fear that they will be judged to have neglected their markets or otherwise exploited their monopoly positions in a non-competitive manner. It also benefits carriers which want to cash in their chips by selling off routes which they can treat as private property. It doesn't really aid carriers which have provided adequate service at competitive prices and wish to continue to do so since their renewals can and should be expedited in any case.

ALTERNATIVES

DOT has under active consideration a rulemaking proposal in which it is apparently considering improved expedited procedures for renewal applications. Transamerica believes that an administrative solution to this renewal issue would be preferable to a legislative one. A rulemaking solution will provide greater flexibility to deal with different situations that cannot adequately be foreseen in legislation such as S. 586. Transamerica cannot, of course, endorse the terms of a rulemaking proposal which it has not seen. However, DOT needs no legislative power to enact such a solution and should be given the opportunity to attempt to do so subject to normal notice and comment procedures.

If a legislative solution is adopted (an action we do not support), Transamerica would prefer a bill such as that put forward by People Express. At a minimum any legislative solution must contain liberal bumping rights which preclude a certificate holder from blocking entry to a route which is not receiving competitive levels of service and pricing. The People Express provisions on this issue (while not perfect) are far preferable to those contained in S. 586.

Senator **Kassebaum**. Senator Inouye.

Senator **Inouye**. Madam Chairman, instead of asking questions I would like to make an observation. The witnesses on this panel have all indicated that the passage of this measure would be anticompetitive, and yet the DOT Deputy Assistant Secretary, Mr. Shane, has indicated that passage of this bill would broaden the authority of the Secretary and give greater flexibility. It would enhance competitiveness. Furthermore, it would deluge their office with more work. Instead of no challenges, they will have constant challenges.

So I do not know who to believe. You say it is anticompetitive. Mr. Shane, who is part of DOT, says it will enhance the competitive nature of this business.

Second, I would believe that, on the issue of competition, to be under scrutiny once every 5 years and being under scrutiny constantly provides an interesting question on competition. I would think constant scrutiny would be much more competitive than scrutiny once every 5 years. And that is my observation.

Thank you.

Senator KASSEBAUM. Does anybody wish to answer that? Mr. Hitchcock.

Mr. HITCHCOCK. I will make an effort. I'm not sure there is the inconsistency. In some respects, the ultimate result depends upon how the legislation is in fact administered, the same way with any piece of legislation. The Secretary has a great deal of latitude to deny applications.

I think I understand the Senator's point that if you are under constant scrutiny that might enhance certain behavior, but that depends on the extent to which there is a credible threat that a new applicant is going to come along and be able to bump an incumbent. And the point that I was making in our testimony is that the standard which a new applicant would have to meet is a very difficult standard: Substantially improved competition, substantially improved service, that sort of thing.

I would agree with Mr. Shane, it is probably true that they would be getting applications in on a regular basis. But the statute makes it very easy, for the Secretary to dismiss them, and it could be administered such that——

Senator INOUYE. Is that not the present day situation, that the Secretary can dismiss the applicants?

Mr. HITCHCOCK. Well, it does not really come up that often. I mean, if you have a 5-year renewal procedure, the analogy that comes to mind—I am not sure how much it is still true—it is like radio or television licenses. It provides a regular basis for challengers or for the agency to assess how good a job the company has been doing over the long haul.

Senator INOUYE. Under the present law, I believe the history shows that in the past 30 years no one has been thrown out.

Mr. COHN. Senator, may I address that? In fact, I think there are a number of examples where carriers have been replaced. In 1978, Pan American had operated and was authorized to operate between the United States and Scandinavia, and the CAB determined in its wisdom that Northwest could provide that service better, and in a renewal proceeding they in fact transferred that authority from Pan Am to Northwest.

Senator INOUYE. Pan Am did not object to that.

Mr. COHN. I do not know whether that is true or not, but in another——

Senator INOUYE. In fact, they wanted to give that up.

Mr. COHN. In 1980 in a renewal proceeding involving Houston-Yucatan TI, Texas International, who was the incumbent and objected quite strenuously, their authority was not renewed and the route was transferred to Continental Airlines.

As it worked out, several years later Continental ultimately picked up the route by buying Texas International, but in fact that was a highly contested case in which the merits of the competitive market structure for serving Yucatan from Houston was litigated and the CAB determined that it would be in the best interests of the traveling and shipping public for Continental to have that route and not Texas International.

Senator **Kassebaum**. Would you yield for just a minute, because I am curious. When you talk about competitive, what criteria, for instance, is looked to in competitiveness? What do you view as important? What did CAB base their decision on?

Mr. **Cohn**. Well, the CAB looks to a number of different economic factors to determine which carrier will enhance competition. Number one, they look to see——

Senator **Kassebaum**. But how do you enhance competition?

Mr. **Cohn**. By having a carrier that will be able to provide greater public service benefits at a particular gateway than some other carrier.

Senator **Kassebaum**. Do you mean better fares or better service?

Mr. **Cohn**. Yes and no. Let me give you an example, if I could, and it could be hypothetical, but it could be very real. If you take the Newark-London route, for example, it is a temporary route. And let us assume that we were to come up for renewal and, People Express being the largest airline right now at Newark, operating over 200 departures a day, feeding traffic from 40 different cities into and out of Newark every day.

And let us assume that there was an applicant, Ajax Airlines, that decided it wanted to compete for Newark-London, Ajax operating one flight a day into and out of Newark, and that is quite possible, or a limited number of frequencies.

Ajax, under the current bilateral between the United States and the United Kingdom, the way the United Kingdom administers it, could not operate any more service than People Express. We are limited essentially in the offpeak season to five trips per week, and we are also limited to approximately one daily, to a somewhat higher, during the peak summer season, two daily service. So our capacity is frozen.

I would doubt very much whether there is any airline in the country that could offer fares lower than People Express. But even if there was, it wouldn't be substantially lower. We started service in the market at a $149 unrestricted economy fare and we kept that for over a year. So the fares are essentially fixed by foreign government also.

The difference between an Ajax and a People Express, where it comes with the competition factor and the consumer enhancement factor comes in, is the fact that People Express is going to be able to benefit and enhance and make its service much more profitable, not only for it but for the traveling public, because it is feeding from so many different regions of the country and providing opportunities for passengers from the Midwest, from the South, from the West, competitive opportunities.

Instead of they will have Newark as an opportunity, an online single carrier service opportunity to go to London instead of going to JFK or Atlanta or DFW. And by selecting a People Express airline at Newark, you are enhancing overall U.S. aviation competition by providing a strong carrier who is able to feed passengers from a number of cities and provide competitive gateway opportunities.

And that is what the DOT and CAB historically looks to in making its carrier selection determinations.

Mr. **MANLEY**. Madam Chairman, it is possible that DOT could, taking your point, be very helpful in this whole process by adopting a rule stating what it believes to be the competitive enhancement factors, so people know in advance 5 years from now what they are going to have to show DOT. If they make that showing, there should be no need to put them through a renewal proceeding. Everyone is going to know they meet the standards; they are automatically turned over.

So you get both constant supervision by reference to these standards, if they will define them, and you get the benefit of having the renewal simplified so that they do not have to worry about someone coming in and starting a frivolous, if you will, case to take over that route, because they are already performing what the Government has defined as competitive service to the extent that is possible where there is not free competition.

Now, if you ask me what those standards are, I really would have difficulty listing them. But I think this is the advantage you would get from a rulemaking proceeding, because they can throw some ideas out, other people can think about them, and help formulate a series of standards for people to know what they are going to have to live by when they come up for renewal.

Senator **KASSEBAUM**. Well, Senator Inouye, I interrupted your question. But the thrust of my comment was really, realizing that fare and service was to a certain extent regulated by the bilateral arrangement, that has always seemed to me to be the heart of competition in what you could offer.

And since that was already predetermined, what actually then was going to be harmful to the consumer necessarily by having it permanent, for instance, because it was frequently out of the hands of those who were competing because of prearranged agreements.

I guess I could see where, if they are going to base it on a competitive market structure as would exist in the domestic market, which is, Mr. Cohn, somewhat I guess what you were saying, that that structure of course is a result of all of the competition that exists here that could enhance one's service abroad. But that largely comes from the competition that exists here and not what would necessarily be benefiting a consumer abroad.

Senator Inouye.

Senator **INOUYE**. Thank you very much.

I would like to make a final observation. When deregulation was adopted as national policy, the promise was that you will have greater frequency of service at lower rates. Taking into consideration the inflation rate, which incidentally is coming down, the regular fare from the West Coast to Hawaii since deregulation has not kept up with inflation or has not come down. In fact, it has increased.

I can see that with the checks I have to send out. It is true that about 3 percent of the seats have come down, because if you are willing to purchase a ticket 30 days before flight time and fly on Tuesday, Wednesday, and Thursday, without having lunch, you can fly cheap. But for regular fares, with all of this competition, No. 1 frequency has gone down, prices have gone up.

And Madam Chairman, if that is competition I hope we come up with something else.

Senator KASSEBAUM. Thank you.

I would have one other question that I would like to ask, because you said, Mr. Cohn, that actually People Express on a temporary certificate has done very well against the holders of permanent certificates in the London—United States to United Kingdom market.

If that is the case, what difference does it make to you?

Mr. COHN. What difference? I am not sure——

Senator KASSEBAUM. Well, you would like a permanent certificate?

Mr. COHN. No, I am not suggesting that at all. I am suggesting that we would benefit by virtue of S. 586 because that temporary certificate would be converted into an indefinite one. But we are willing to forego that benefit because we see it in our long-term best interest. I would rather have a structure that keeps my certificate temporary and all of the other certificates temporary, to give us opportunities to expand our international routes.

Senator KASSEBAUM. But it has not kept you from expanding, has it?

Mr. COHN. No, it has not, except that if you were to convert temporary certificates in limited entry markets into indefinite certificates it will make it much more difficult for People Express to obtain the valuable limited entry routes that will be held by those carriers who are now holding indefinite, just as it would make it very difficult for a new carrier to obtain our Newark-London route.

We recognize that that would be a barrier and would protect us to some degree from the rigors of competition. But I am willing to forego that.

Senator KASSEBAUM. But does that have anything to do with whether it is permanent or temporary?

Mr. COHN. Very much so, and the reason is that from a surface point of view you could look at the legislation as attempting to achieve the same objective through different ends. You either make them temporary and have them subject to renewal under certain standards or you make them all indefinite with a liberal bumping mechanism. And ideally, you want to achieve the same result, which somehow is to replicate competition, to keep the industry honest, to provide opportunities for new carriers.

The problem is—and I think Mr. Shane has underscored that today, perhaps indirectly—is that there is an administrative inertia against taking actions unless they have to, and that is the historical Government way of life; and that if there is no renewal the Government will wind up figuring a number of different ways how not to do something. And I suspect that if you have an indefinite certificate regime with bumping mechanisms, it will be very difficult to overcome that administrative inertia, for new carriers to knock on the door of DOT and say, please set down a case, particularly when you have a very liberal ability to dismiss with impunity, without any ability basically to go to court and overturn that dismissal.

Senator KASSEBAUM. I think Senator Inouye's point about the bumping mechanism being something that is an ongoing process rather than just a review every 5 years a good one. The criteria is one that can be either DOT developed, which I think is important, or through a measure which closely tracks DOT's.

It would seem to me at that point you would have adequate protection, I would think significant for consumer protection, and any benefits from competition.

Mr. COHN. Well, that is why we proposed an alternative in our testimony that would in our view attempt to track the bumping standard to the carrier selection standards used by DOT, while that is kind of a second best. We prefer the current regime, but if you are going to an indefinite duration certificate regime we think that bumping standard could work, assuming it is administered properly by the agency.

Mr. HITCHCOCK. One final thought, if I may. You are really juggling here with two competing interests. On the one hand, the carriers who do win a route say they want enough time to develop routes, particularly those that might not initially be profitable. They may want several years, and they have traditionally said they want certainty in order to have a chance to develop a market.

On the other hand, there is the goal in the proposal being discussed of assuring there is some chance of being bumped. I think that if you have fixed terms of five-year increments or 7-year increments, I think as the FCC used to do, you have managed to accommodate those two concerns.

If you do conclude that it is better to have the possibility of challenges on an irregular basis or when even a new challenger wants to come along, there is a question of how do you balance things such that an application is a credible threat to carriers not doing a good job and that somebody new can come in. And the point that I was making—I think the other two gentlemen were, too—is that the standard here may be administered in a manner that it does not provide that much of a credible threat.

Senator KASSEBAUM. I certainly thank the panelists. It does seem to me an interesting question, and it has been raised here today, about permanent international route certification at the time of a sale and how that is handled. And I think that that is a very crucial question to be addressed.

Senator Inouye, do you have anything further?

Senator INOUYE. I would like to thank you, Madam Chairman, for scheduling this hearing. I appreciate it very much.

Senator KASSEBAUM. Well, I would just say to you, Senator Inouye, that I think bringing S. 586 forward is an important step, and at least it will focus the issue and perhaps because of that we will resolve what could grow to be ever thornier questions.

Thank you. That concludes the hearing.

[Whereupon, at 12 noon, the hearing in the above-entitled matter was adjourned.]

ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

STATEMENT OF CLARK H. ONSTAD, VICE PRESIDENT FOR GOVERNMENTAL AFFAIRS, CONTINENTAL AIR LINES, INC.

Madame Chairwoman and Members of the Subcommittee, I am Clark Onstad, Vice President for Governmental Affairs of Continental Air Lines, Inc. I appear today to express Continental's strong opposition to the proposal to convert "temporary" international route certificates into "permanent" certificates. Continental opposes the proposed legislation despite the fact that it has substantial temporary international route authority that would be made permanent were the measure to be enacted.

S. 586 is special-interest legislation that would have very significant anti-competitive impacts on international air transportation. By granting permanent certificates to a few entrenched air carriers at the expense of competition and the traveling public, S. 586 threatens to withdraw many of the pro consumer gains that have been made in an area that naturally tends toward profectionist government regulation. In our view, no compelling reasons have been advanced for seeking to insulate international markets from the limited competitive pressures created by the award of temporary-experimental certificates.

International air service today can best be described as a shared monopoly. Many carriers holding permanent certificates have little incentve to improve service or offer options that would benefit the traveling public. If we are to avoid abuse of the market power held by incumbent carriers, competitive pressures must somehow be maintained. The single most effective means to maintain competition in the international aviation system is the temporary certificate.

Indeed, the question which this subcommittee should be examining is whether all international certificates should be made temporary or of limited duration. Why shouldn't the holder of a certificate periodically bear the burden of proof in demonstrating the quality of the service it has provided to the public With respect to both of these questions, S. 586 appears to propose an abrupt departure from the policy of and trend toward competition based upon deregulation and reduced barriers to entry.

I. CONTINENTAL AIR LINES' PERSPECTIVE.

Continental Air Lines has had extensive involvement in various international aviation regulatory proceedings. This experience has proven the merit of the temporary certificate; it has also laid to rest many of the arguments put forth by the advocates of permanent international certificates.

Over the past few years, Continental has successfully challenged the renvewal of the authority of an incumbent carrier on an international route in a certificate renewal proceeding. Most recently, Continental won the right to offer low fare, competitive service to London, England from Houston, Texas. Our competitor for the Houston-London route, Pan American World Airways (Pan Am), already held a temporary certificate authorizing it to offer service in the market, and was the designated U.S. carrier under the binding bilateral agreement. However, Pan Am had suspended Houston-London service in 1982. Pan Am showed no interest in reinstating non-stop Houston-London service until Continental announced its desire to serve the route.

Continental inaugurated Houston-London service on April 28, 1985 carrying passengers from Houston and the thirty-six feeder cities served by Continental from which London traffic is drawn. Within five days after beginning to take reservations, Continental had recorded more than 50,000 booking segments, or 25,000 round trips, representing savings to the consumer of $10 million. This is graphic evidence of the value of temporary international route awards.

II. TEMPORARY-EXPERIMENTAL CERTIFICATES ARE AN EFFECTIVE WAY TO BRING THE BENEFITS OF COMPETITION TO INTERNATIONAL AIR TRAVEL

Permanent certification as proposed in S. 586 would eliminate a meaningful opportunity for effective competition in the provision of international air service to many of the world's most important markets. Without the automatic review afforded by temporary certificates, the only opportunities left for a new carrier to offer service in a limited entry international market would require reliance on the benevolence of the governments. The Government would be called upon to assist either through a cumbersome and necessarily infrequently used "bumping" procedure to revoke the certificate of an established carrier or, in an even more unlikely event, in international negotiations that would produce an agreement with a foreign government to permit additional carriers to serve a particular destination.

The difficulty of convincing a regulatory agency to revoke a permanent certificate, both under the existing procedure of section 401(g) and the proposed procedure of S. 586, presents very substantial barriers. Because of these barriers, petitions for removal of an incumbent carrier have rarely been filed, and even more rarely granted. Past practice demonstrates that such "bumping" procedures are ineffective to stimulate competition because they do not present a realistic threat of new entry. The burden placed on a carrier seeking to replace an incumbent is so extreme that such carriers are simply not given an equal opportunity to win the certificate through fair competition.

Because of the existing international aviation regulatory system, strategies to bring the benefits of competition that work in the domestic marketplace simply cannot be applied to the international aviation market. Therefore, a regulatory procedure must be made available that will provide at least some of the benefits that flow from a competitive system to the international airline passenger while regulatory intrusion is kept to a minimum. That regualtory device has been the award of limited duration temporary certificates to engage in international air transportation.

The temporary certificate has been described by the former Chairman of the CAB, Dan McKinnon, as a "regulatory substitute" for the market pressures that a truly competitive environment in the provision of international air services would bring to bear. It has been described as an incentive to make carriers responsive to consumer demand, as well as an incentive to encourage competition by other carriers with potentially superior fare and service plans.[1]

Automatic review through the temporary certificate award and renewal process is a major performance incentive for carriers. For example, when Continental sought to replace Western on the Texas/Alberta/Alaska route, Western's service suddenly improved significantly.[2] Had Western not held a temporary certificate subjecting it to possible competition from Continental for the route, would that service have been improved? If the incumbent's carrier's past performance had not been subject to careful scrutiny by the regulatory agency in the route renewal proceeding, would the public have had access to better service? The mere threat of a challenge in a renewal proceeding thus operates more effectively than any increased level of government scrutiny or possibility of certificate revocation, termination or suspension to avert exploitation of the airline customer and monopoly practices by incumbent carriers.

Even in the highly regulated international market, there is ample room for competitive considerations. The federal government has a responsibility, as expressed in both the Airline Deregulation Act of 1978 and the International Air Transportation Competition Act of 1979, to regulate international air service in a manner that will encourage competition. In making initial international route awards, the CAB judged route applications to determine what consumer benefits would be produced, as reflected in fare and service proposals. In choosing international gateways, the CAB strived to encourage regional competition among different carriers serving different gateways (the intergateway competition policy), as well as to encourage the maintenance of competitive pressures on the overall international structure through the selection of U.S. flag carriers and United States gateways. The temporary certificate and conditions commonly attached thereto[3] were described by the CAB as an

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[1] *See* 47 *Fed. Reg.* 32443 (1980).

[2] Continental did ultimately win authority to serve Texas/Alberta markets; service was instituted in March, 1985.

[3] A typical temporary-experimental certificate provides that "The holder acknowledges that this certificate is granted to determine if the holder's projected services, efficiencies, methods,

Continued

important part of this effort, necessary to apply regulatory pressures on carriers that are otherwise protected from competition by bilateral aviation agreements.[4]

In addition to substituting for traditional competitive pressures by encouraging better performance by incumbents, the temporary certificate also offers the prospect of improved service through the choice of a new carrier in a renewal proceeding. A carrier seeking to replace an incumbent in a market may have substantial incentives to develop a service and amenities program that will be more attractive to passengers. A new carrier may offer a fare structure which, although subject to foreign government approval, acts as a spur to increased travel that will encourage market growth. A new carrier may be more willing to offer these incentives to gain acceptance in the market than an entrenched incumbent with no particular incentive to do anything to attract what is essentially a captive market of passengers. A new carrier may be more willing to concentrate its efforts on marketing and developing a route.

What does entry by a new carrier into a market mean? For Continental's Houston-London passengers, it has meant reductions in the established first class, business and coach fares of 39%, 8% and 42% respectively. Overall, consumers will save well in excess of $10 million when Continental's fares are compared to the fares British Caledonian charged on the route prior to Continental's entry. Equally important, on-line service is now available to many cities that never previously enjoyed such convenience.

In contrast to this example of the benefits of introducing competitive new international service, the pending proposal by Pan Am to sell its Pacific division to United Airlines (United) presents the most pronounced example of the evils of permanent route awards. Pan Am acquired most of the route authority it proposes to sell to United thirty to fifty years ago, when Pan Am was viewed as the "chosen instrument" of U.S. aviation policy. Over this long period there has been no critical reevaluation of the competitive implications of introducing service by other carriers into these routes. This is so despite significant changes that have occurred in U.S. bilateral aviation relationships with Japan and emerging trade relationships in the Pacific Basin, which may be severely disrupted if the proposed route sale is approved.

The route sale proposed by Pan Am involves authority spanning one-third of the globe. It is incumbent upon the U.S. government to review the competitive implications of such a transfer. Yet we are today faced with a proceeding that will review only whether the agreement violates traditional antitrust standards, not whether there are alternatives to the proposed sale that will have materially less anticompetitive effects. This failure to give a full hearing to competitive issues is direct outgrowth of Pan Am's "permanent certification" on these routes, without which the sale would undoubtedly not even have been attempted.

III. THE CLAIMS OF NECESSITY FOR THE LEGISLATION ARE UNSUBSTANTIATED.

A number of arguments have been advanced to support the granting of permanent international aviation certificates. On closer examination, it is aparent that none of these arguments constitutes a sufficient basis for enactment of an anti-competitive policy by this Congress.

Congress has been told that the temporary certificate renewal process is an unnecessary, expensive and burdensome regulatory proceeding. Continental disputes these characterizations. If route proceedings are in fact as costly as some of the current certificate holding carriers allege, many competitor airlines would be unable to make a credible challenge to the reissuance of a route award. That many carriers stand ready and willing to make this challenge belies the validity of the incumbents' assertion.

Nor is the administrative process leading to certificate renewal excessively burdensome. Indeed, the mechanism proposed in S. 586 for challenging incumbent carriers promises to be more burdensome and more lengthy than a regular renewal proceeding. In the renewal context, expedited methods of proceeding, including the use of show cause orders where there is no challenge to an incumbent and other expedited procedures are available. In contrast, a "bumping" proceeding would almost always involve a full scale evidentiary hearing, with attendant expense and time delays.

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rates, fares, charges, and other projected results will in fact materialize and remain for a sustained period of time, and to determine whether the holder will provide the innovative and low-priced air transportation it proposed in its application for this authority."

[4] *See, e.g.*, Wild Card Route Case, Order 80-3-170 (February 27, 1980) at 12.

Some carriers also complain that the policy on the award of international route certificates has been applied inconsistently. The clearest solution to such a problem is simply to impose a uniform system applicable to all certificates, with no grandfathering of any certificates—all certificates should be made temporary.

Carriers that would benefit from this legislation argue that limitations on the duration of certificates might prohibit them from recouping investments made in facilities, equipment and other aspects of international service. This contention is plainly without merit. One of the biggest problems facing the aviation industry today is airport access, both in the United States and abroad. Given this, it is difficult to conceive of a situation in which a new carrier on a route would not be confronted with the problem of scarce airport resources, including facilities, gates and terminal space. This scarcity assures that facilities will certainly be sold at cost by carriers leaving international routes. Indeed, experience teaches that such facilities will often be sold at a significant premium. It is also interesting to note in connnection with this issue that since the CAB began awarding limited duration certificates, the question of whether an investment can be recovered within the limited term of the temporary certificate has not presented any apparent disincentive to carriers eager to offer new international service.

Proponents of S. 586 suggest that there is really no room for competition in limited entry international markets, since fares and frequencies of service proposed by new carriers seeking to serve international markets will require approval of foreign governments. This should not be seen, however, as imposing any absolute ban on competitive services. Rather, it should be viewed as an opporntunity for this country to aggressively support the pro-competitive service options set forth by U.S. carriers seeking entry into foreign markets.[5]

Another argument raised by supporters of this legislation is that foreign carriers do not have to undergo route renewal proceedings, and that U.S. flag carriers would be put at a competitive disadvantage vis-a-vis their foreign competitors by undergoing a renewal proceeding. If foreign governments whose aviation policy relies less on competition wish to insulate their carriers from renewal proceedings, the U.S. can do little to alter their outlook. This does not, however, offer a sound basis for insulating U.S. carriers from legitimate competitive pressures, which will likely result in improved service by the U.S. carrier and hence a stronger competitive position with foreign flag carriers.

IV. CONCLUSION.

The international air traveler has the same right to high quality air service as does the domestic passenger. However, the unfortunate characteristics of the international air travel market are such that the beneficial aspects of free and open competition in the provision of air transportation are less likely to be available to the international passenger. Temporary route certificates are the regulatory means that has been developed to introduce at least a modicum of competition into this industry. By putting carriers on notice that their service will be periodically reexamined, and by opening their authority to challenge by a potential competitor, temporary certificates do more than any other type of regulatory structure to protect the public interest. Granting permanent route authority to a select group of established carriers, on the other hand, runs directly contrary to the pro-competitive mandates of U.S. aviation policy.

Statement of the City of Houston and Houston Chamber of Commerce

Madame Chairman and Members of the Committee: The City of Houston and Houston Chamber of Commerce ("Houston Parties") hereby submit this written statement for the record on the issue of whether temporary international certificates issued to U.S. carriers by the Department of Transportation ("DOT") should be converted into certificates of indefinite or permanent duration. The specific legislation which proposes to accomplish this, and which is being considered by the Subcommittee, is S. 586. The Houston Parties have in the past supported maintaining the current policy of issuing temporary certificates in "limited-entry" markets because of their belief that the temporary nature of certificate awards is the most efficatious regulatory substitute for the self-disciplining forces of competition. However, the Houston Parties could conceivably accept such a proposal if it were accompanied by a liberal, workable and *meaningful* mechanism whereby a carrier holding a permanent international certificate could be "bumped" by a more worthy competitor. The Houston Parties most respectfully oppose S. 586, because it contains a wholly inadequate "bumping" mechanism, and would, in effect, provide certificate holders in limited-entry international markets with a regulatory windfall and lasting protection from competition.

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[5] The CAB explicitly recognized this point. While acknowledging that fares or service proposals may be rejected by foreign governments, the CAB expressed its wish to encourage carriers to go forward with innovative low fare proposals, and to reflect such proposals in the negotiating priorities of the U.S. in bilateral aviation talks. *See* Wild Card Route Case, Order 80-3-170 at 8 (February 27, 1980). The Board has also stated: [w]e recognize that diplomatic considerations may impede or even prevent the implementation of a carrier's fare and/or service proposal. . . . fares lower than those currently offered in the markets may not be approved. But the mere possibility of objections by [a foreign government] does not lead us automatically to discount [a potential carrier's] low fare proposal. Rather, we will weigh each applicant's proposal or failure to propose low fares as indicative of its willingness to mount a competitive challenge to [foreign flag] carriers and to press with us for liberalization of [foreign government] fare policies. Texas/Great Lakes-Eastern Canada Service Case, Order 80-5-91 at 6 (May 13, 1980).

This Subcommittee has already heard testimony establishing the main justification for issuing temporary certificates to carriers serving limited-entry markets: that since entry into these markets is by definition limited by foreign governments the only way to insure that such carriers are subjected to some form of competitive pressure is to issue them fixed-term, temporary certificates. This allows competitor carriers the opportunity, in a certificate renewal proceeding, to attempt to demonstrate that they could provide better service than the incumbents in those markets. The Houston Parties endorse these arguments wholeheartedly, and note that temporary certification has the following public benefits in these circumstances. First, it encourages more honest and reasonable applications for certification of service to limited-entry markets, since carriers will eventually be forced to explain, in a certificate renewal proceeding, discrepancies between the service which they had proposed and the service which was actually provided. Second, it ensures that the certificated carriers in such markets will heed consumer preferences and demands, so as to justify their continuing to be certificated on the route. Third, it provides other carriers with the opportunity to show whether and how they could provide superior service to that being provided by the incumbent, and therefore serve the public interest.

As noted above, these goals could be achieved by issuing permanent certificates for limited-entry markets *only if* DOT is provided with an effective mechanism whereby it can "bump" a certificate holder. The "bumping" mechanism contained in S. 586 would not serve this purpose; it establishes decisional standards which would make it virtually impossible for any carrier to effect a replacement. S. 586 requires the applicant for such replacement to demonstrate that it can and will provide substantially improved service and fares. Since fares and/or capacity are stringently regulated by foreign governments in many limited-entry markets, applicant carriers most likely could not in good faith argue that they would be able to reduce fares or increase service, even if the quality of the service which they could provide would be vastly superior to that of the incumbent. The Houston Parties endorse the proposal already advanced to the Subcommittee that such "bumping" standards be keyed to the decisional criteria used by DOT in carrier selection route cases. This would allow an Applicant the same opportunity to obtain certification for a valuable limited-entry route as it would have if the route were being authorized for the first time.

It should be noted, however, that even though a workable "bumping" mechanism would, in theory, serve to maximize the role of competitive market forces in the designation of U.S. carriers for international routes, the practical problem of "administrative inertia" could still limit the effectiveness of such a mechanism. DOT would be under no pressure to act on a carrier's application to replace the holder of a permanent certificate, as it is when faced with a renewal proceeding. The Civil Aeronautics Board demonstrated an unwillingness to replace a carrier designated to serve a limited-entry market unless the carrier has terminated service or its temporary certificate is soon to expire—even in circumstances in which the carrier has reneged on its route-case promise and had not fully used their authority in limited-entry markets.

For example, Western Airlines received authority from the Civil Aeronautics Board to provide nonstop service on the Houston-Alberta route, but never provided such service. Nonetheless, the CAB refused to consider a petition by Continental Airlines to replace Western on the route. It was only when Western pulled out entirely from the market that the CAB replaced it with another carrier. Otherwise, there would have been no service over the route until Western's certificate expired and the Board was forced to act. Similarly, when Pan American World Airways suspended service between Houston and London in 1983 and routed all U.S.-London service over its New York gateway, the fact that it had to renew its certificate was the only effective vehicle by which the service issues in this important Houston market were resolved.

Thus, the practical result of converting temporary certificates into indefinite or permanent certificates, even with subtantatively liberal "bumping" standards, could simply be that incumbent carriers would retain their certificates indefinitely because of mere administrative non-action. Therefore, the Houston Parties still maintain that the best way to ensure that consumers and cities receive the maximum benefits is simply to continue to impose temporary certificates on all carriers serving limited-entry routes.

The Houston parties appreciate the opportunity to submit their views on this important aviation policy issue.

STATEMENT OF GENE E. OVERBECK, SENIOR VICE PRESIDENT, GOVERNMENT AFFAIRS, AMERICAN AIRLINES, INC.

American Airlines opposes enactment of S. 586 in its current form. There are no good reasons why temporary certificates of United States air carriers relating to international air transportation should be made permanent or indefinite through legislation.

Although it is claimed that temporary certificates have historically been renewed more or less automatically, and that the legal fees generated by renewal proceedings are a waste of money, such claims are not compelling. Indeed, the expense of renewing a certification will probably vary inversely with the strength of the incumbent carrier's case for renewal.

There are two good reasons why the bill is not in the public interest. The first is that permanent certificates encourage route trafficking. The second is that permanent certificates make it difficult for the Department of Transportation to replace an incumbent carrier when changed circumstances warrant such replacement.

ROUTE TRAFFICKING

Permanent route certificates are more likely to be regarded as balance sheet assets than temporary ones, and thus more likely to be bought and sold. Braniff designated its succcessor in South America by means of selling its route certificates in 1982. Pan Am now proposes to do the same in the Pacific.

One of the Committee's goals should be to insure that the designation of successors on international routes be the responsibility of the Department of Transportation, and not the carriers who elect to abandon service on these routes. If Braniff's South American certificates and Pan Am's Pacific certificates were all temporary ones, it is less likely that they would have become the subject of sale negotiations.

In designating successors, the Department of Transportation may be expected to maximize competition between gateway cities to any given international destination. Incumbents who decide to sell international route authorities will have no reason to foster gateway competition because to do so would only reduce the price.

It is ironic that TWA is urging that its certificates be made permanent at the very time that it is struggling to avoid a takeover by Carl Icahn, who presumably would like to engage in some route trafficking. If all TWA's certificates were temporary, that carrier would be a less attractive proposition to the likes of Mr. Icahn.

CHANGED CIRCUMSTANCES

In the wake of deregulation, the domestic route structures of many international carriers have changed dramatically. In some cases, these changes may well dictate replacement of an incumbent carrier on an international route.

For example, TWA does not today have the same relative presence in Chicago as it did when it first received Chicago-London authority more than 25 years ago. In the years ahead, TWA may well retrench further in Chicago as it expands its St. Louis hub. Indeed, TWA has only recently inaugurated St. Louis-London service. Under these circumstances, it is difficult to comprehend why TWA's temporary certificate for the Chicago-London route should be made permanent.

RECOMMENDED REVISIONS

American Airlines would not oppose enactment of S. 586 if it were amended to take into account the possibility that changed circumstances may dictate replacement of an incumbent carrier on an international route. However, the "bumping" provision contained S. 586 falls short of the goal. By way of illustration, it does not provide an appropriate basis for designating a replacement carrier on TWA's Chicago-London route. The rationale for such replacement would not be "a substantially improved combination of service and fares" by the replacement carrier. The true basis for such action would be that TWA's lack of sufficient feed at Chicago has diminished its ability to provide strong competition to British Airways in Chicago and to other U.S. carriers operating over alternative gateways to London, and that the replacement carrier would correct these deficiencies.

An alternative "bumping" provision that would provide a better mechanism for designation of a replacement carrier under such circumstances is set forth in the Attachment hereto.

CONCLUSION

There is nothing inherently wrong with temporary certificates. To make all temporary certificates permanent, in the manner proposed by S. 586, would serve no valid purpose.

ALTERNATIVE "BUMPING" PROVISION

The Secretary of Transportation may, upon application or upon the Secretary's own motion, review the authority of the holder of a certificate to provide the foreign air transportation described therein. If the Secretary finds, after notice and hearing, and after consideration of the same carrier selection criteria that would be considered in a de novo route case, that the certificate holder is no longer the air carrier best able to serve the route or routes in question, and that another air carrier who is materially better able to serve the route or routes has applied for authority and is ready and willing to commence such service, then the Secretary may suspend the authority of the holder, modify or suspend the holder's certificate and grant authority to such other air carrier.

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